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OIL MERGER ACTIVITY

HEARING

BEFORE THE

COMMITTEE ON THE JUDICIARY
UNITED STATES SENATE

NINETY-EIGHTH CONGRESS

SECOND SESSION

ON

THE REASONS FOR CURRENT MERGER ACTIVITY WITHIN THE OIL INDUSTRY AND ASSESS THEIR EFFECT ON THE NATION

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OIL MERGER ACTIVITY

THURSDAY, MARCH 15, 1984

U.S. SENATE,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The committee met, pursuant to notice, at 2:15 p.m., in room SD-106, Dirksen Senate Office Building, Hon. Strom Thurmond (chairman of the committee) presiding,

Also present: Senators Hatch, Specter, Metzenbaum, and Heflin.

Staff present: Vinton DeVane Lide, chief counsel and staff director; Steve Cannon, chief counsel for antitrust; Joseph Gibson, research assistant; Karen Gordon, staff assistant; Renn Patch, Randy Rader, and Steve Markman, of Senator Hatch's staff; Mary Louise Westmoreland, of Senator Specter's staff; Steve Ross and Doug Lowenstein, of Senator Metzenbaum's staff; and Arthur Briskman, of Senator Heflin's staff.

OPENING STATEMENT OF CHAIRMAN STROM THURMOND

The CHAIRMAN. The committee will come to order.

Today the committee turns its attention to mergers. In recent weeks, national attention has been focused specifically on merger activity within the oil industry. Congressional interest in this subject has been particularly intense. As chairman of the committee on the Judiciary, I felt it not only appropriate, but rather imperative, that the committee initiate hearings to both study the reasons for these mergers and carefully assess their effect.

Critics of these recent mergers have argued that they discourage exploration for new oil, produce an intolerable drain on our capital markets, and have both horizontal and vertical anticompetitive effects. Consequently, a moratorium on oil merger activity is being urged. Opponents of any moratorium argue that such legislation would constitute an unwarranted interference in free market forces and that our current antitrust laws are sufficient to prevent anticompetitive mergers.

The task the committee faces is to air this issue thoroughly in order to determine what course of action, if any, is truly in the public interest and fair to all concerned. The questions we examine today are very complex and of immense importance. I would therefore urge my colleagues on both sides of this issue to exercise great care. The committee will continue to fulfill its responsibility to provide advice and counsel to the Senate on this and all other antitrust issues.

The Senator from Ohio, do you have an opening statement?

OPENING STATEMENT OF SENATOR HOWARD M. METZENBAUM

Senator METZENBAUM. Mr. Chairman, first I want to compliment you for holding this hearing and actually for accelerating the dates of the hearing, because I think there is a sense of urgency, and I am glad that you saw fit to do just that.

Mr. Chairman, the corporate takeover game has a language of its own. Shark repellent, poison pills, golden parachutes, scorched earth, and so on. In recent weeks, a new phrase has been added to this colorful list, and I call it the oil slick.

In this tactic, one large oil company acquires another large oil company and all that is left is a thick slick residue symbolizing a great company that will never be again.

The most recent practitioners of the oil slick tactic are Texaco and Getty, Socal and Gulf, and Mobil and Superior. I want to make it clear when I talk about oil slick, I certainly, in no way, either by inference or otherwise, suggest any impropriety on the part of those who are involved.

As a matter of fact, it should be noted that these companies have all acted lawfully. Their executives have honorably pursued legitimate business ends, and I find no fault with that.

The responsibility is that of us in Congress. The men who run these companies have a right to proceed under the laws as they exist. We, in the Congress, have an obligation to change those laws if we do not think they are in the Nation's best interest.

But the fact is that unless we in Congress act to change the law, we may soon add a half dozen more companies to the list of firms that once occupied proud and prominent places in the oil business.

It used to be the oil companies went south, west, and north to Alaska's challenging frontier to find new oil. Now, they have gone east to Wall Street. Now, they are prospecting for oil in the board rooms of their former competitors.

Five years ago, Senator Kennedy and I authored legislation to ban mergers between the Nation's largest oil companies. This committee favorably reported that bill, but the full Senate never acted. If it had, we would not be here today.

The fact is that the merger ban made sense in 1979. It makes even more sense today. Over the last 5 years, five major oil companies have been acquired through mergers, often by oil companies.

Today, two more megamergers are pending. Frankly, I believe the most recent mergers between Texaco and Getty, Socal and Gulf, and Mobil and Superior are an obscene perversion of the free enterprise system, and the responsibility for those mergers must fall at the doorstep of us in Congress.

Free enterprise has always had a special meaning in this country—the courage to take risks, to pursue and build a dream, to create jobs. That is what it meant to the pioneers, to the giants of the industrial revolution, to the wildcatters and prospectors who helped build our energy industries.

But to today's corporate goliaths, free enterprise means something else. It means the freedom to gobble up competitors, to spend billions to acquire a sure thing rather than to take risks. In a real sense, we are faced today with the choice of what kind of free enterprise system we want.

Since 1979, the Nation's top 20 oil companies have made 11 acquisitions of more than a billion dollars each. The total of these 11 acquisitions alone was $50 billion. Now, we add to that list Texaco-Getty to the tune of $10 billion, Socal-Gulf to the tune of $13 billion, and Mobil-Superior to the tune of $6 billion, bringing the total to about $80 billion.

At the same time these oil mergers were occurring, the industry was spending a great deal of time lobbying Congress. "Preserve the oil depletion," they said, "and we will have more money for exploration." So Congress did. "Preserve the intangible drilling deduction, and we will have more money for drilling." So Congress did. "Give us oil price decontrols and we will have more money for exploration." So Congress did. "Give us special tax breaks for oil shale development." So Congress did. "Give us special tax breaks for synthetic fuels development." So Congress did. "Roll back the windfall profits tax." So Congress did that, too.

Since 1981, the depletion allowance and the intangible drilling deduction alone have poured $22 billion into oil industry coffers with another $20 billion on the way over the next 3 years.

Decontrol has helped push the domestic wellhead price from $13 in 1979 to $27 in 1983. While cabbage-patch dolls sales soared, oil patch drilling declined. The number of rigs operating has dropped every year, and we are producing less crude oil today than in 1973. So where is all the money going?

That brings us to the little game of corporate one-upmanship we have seen in recent months. The money is going to finance takeovers, not exploration and production. It is going to finance acquisitions which have nothing to do with efficiency, with risk, with job creation, or new development.

Indeed, the companies tell us that they are acquiring existing reserves because it is cheaper than finding oil and because there just is not that much more oil to be found anyway. Now, I find that quite curious.

I recall hearing these same executives clamoring for Congress to lease every square inch of the Outer Continental Shelf as fast as possible. I also have a distinct memory of oil company officials demanding natural gas price decontrol so that they would have the incentive to develop the bottomless pool of natural gas reserves in this country. Now, which is it?

Let us examine the most recent mergers. The Socal-Gulf merger and Mobil-Superior deals would be laughable if they were not so disturbing. In the case of Gulf, we have a company that, in the words of Business Week, took a supercilious stance toward a possible raider and then did practically everything wrong to defuse the situation, and that is Business Week speaking.

Now, that company is trekking around the Senate saying that all things considered, it would have preferred its independence but under the circumstances please do not let us fall into the grasp of Boone Pickens. Frankly, I find that rather unseemly.

Then there is Mobil-Superior. This story reads like the pilot for "Dallas." We have a bitter family feud. A corporate chairman so petty that he will not let his own brother ride in the corporate jet. A sister who battles her brother for control while saying to Mr. Pickens, "I should have pushed that Learjet cowboy into the swim-

ming pool while I had the chance." Again, it would be funny if it were not so pathetic.

Mr. Chairman, I believe these mergers pose a real danger to this country. They raise serious questions about competition at all levels of the industry. In the last 5 years, seven oil companies have been gobbled up. Seven more are prominently mentioned as future candidates for the oil graveyard.

We may wake up one morning and discover where there were once 20 or 30 competitors in the industry, there are now only 5 or 10. The mergers also undermine our search for energy independence, and that is probably the most critical aspect of the whole issue.

Here is Socal, historically a vigorous explorer, suddenly raising its debt-to-equity ratio from 7 percent to 40 percent. That will inevitably affect its ability to borrow for future exploration. The same is true of these other takeovers.

The sad fact is that the biggest beneficiary of the takeover boom may be the OPEC nations. Every barrel of oil which is not discovered in this country means another barrel coming from OPEC, and if we have learned anything over the last decade, it is that the OPEC countries are not the ones we should be relying on for our future oil supplies.

It goes without saying that if we have to go back to OPEC and increase our purchases, if we have less domestic production in this country, then the consumer is the one who will ultimately suffer the most, and I think it is the impact upon the consumer with respect to these megamergers that is of critical importance to this Nation. If we add to the cost to the consumer and add to the rate of inflation in this Nation, then we have, indeed, performed a disservice and Congress has failed the people in its responsibilities.

Mr. Chairman, at a later point, and I understand that Senator Johnston will be the next spokesperson, he will address himself to the fact that he and the distinguished Senator from New Hampshire and I will offer an amendment to the bill that is pending before this committee, and Senator Johnston in his testimony, I understand, will explain the specific terms of that amendment.

Mr. Chairman, I thank you very much.

The CHAIRMAN. The distinguished Senator from Alabama.

OPENING STATEMENT OF SENATOR HOWELL HEFLIN

Senator HEFLIN. Mr. Chairman, I am interested in the proposed legislation which I understand calls for a 6-month moratorium. Now, I think we should consider the purpose of a 6-month moratorium.

What is the purpose of Congress looking at this over a 6-month period?

I think there are a number of questions we have to ask. What will be the result? Will we change the antitrust laws? Will we change the Clayton antitrust law? Will we change some function of the procedural method by which the Federal Trade Commission acts or the Department of Justice?

I have yet to hear of the defects in existing law and I hope that the witnesses would express the defects. Now, I also think that we

should ask ourselves what this moratorium will cost the American public.

I believe in competition. I believe in a free enterprise system. Perhaps the greatest example of our antitrust laws has been in the AT&T Co., and hopefully we are going to have more competition in telephone service.

As far as I can see the competition is going to be in long-distance telephone service. But for the sake of saying that we needed to do something about antitrust, it appears that the American public's telephone bills will be doubled from now to eternity.

I think whatever we look at and whatever we do, we should look at it from the beginning and see what the result would be from our actions, what specific laws need to be changed, is there a threat, what is the percentage of the oil reserves that are vested in one company or two companies, and a number of different things that would arise.

I think there are a lot of questions that are raised by this, and I think that these questions need a very thorough examination before we take action that could stop oil drilling for 6 months, that could also be expensive to the American public.

I am open-minded. But there are a number of legitimate questions that are raised by this proposed legislation.

The CHAIRMAN. Thank you very much, Senator.

Now, we have a long list of witnesses here today, 13 or more witnesses. We are first going to hear from the Members of the Senate and if there are any House Members here, we will hear from them.

I think we will have to put a limit of 10 minutes on all witnesses except the Senators.

Also, Senator Dole has a statement he wishes to be placed in the record.

We will take a recess to allow Senators to go vote.

[Whereupon, a short recess was taken.]

[Prepared statement of Senator Bob Dole follows:]

PREPARED STATEMENT OF SENATOR BOB DOLE

Mr. DOLE. Mr. Chairman, I appreciate this opportunity to briefly comment on the recent proliferation of merger activity in our nation's petroleum industry. What appears to be underway is a Major restructuring of this massive industry that will undoubtedly impact significantly not only upon the workers and consumers in my State of Kansas but in every State of the Union. I commend the committee for taking this initiative to delve into these complex issues early on so that we in Congress can be fully apprised as to the ramifications of increased concentration in the petroleum industry. This will surely assist us in our deliberations as to whether any new legislation is needed in regard to these matters.

ANTITRUST CONSIDERATIONS

Mr. Chairman, the potentially negative impact of any large company merging with or buying out a competitor is obvious. From an antitrust standpoint, an increase in market share through acquisition can result in such a diminution of effective competition that protections against artificially high prices and supply control which are built into the concept of free market commerce are lost. The potentially big loser is, of course, the consumer, who may well end up paying higher prices and having less choice concerning the who, how and where of buying a particular product. Of no less importance is the effect mergers in the oil industry or any other industry for that matter, have in human terms, the loss of jobs, the modification of health and pension benefits for employees of companies involved and the financial impact the mergers can have on local communities.

Mr. Chairman, I highlight these dangers not to indicate at this time support for a position that every proposed merger in the oil industry is bad for this Nation and should be prohibited, but to make the point that Congress should take a hard look at these issues to be sure that such transactions now being proposed and those that will surely come forth in the future are properly scrutinized.

TEXACO/GETTY MERGER

I have recently had the opportunity to review the Federal Trade Commission's policy and guidelines in this regard in relation to the proposed Texaco/Getty merger. As part of the FTC's tentative approval of that acquisition, Texaco must within a certain period of time divest itself of a Getty refinery (along with supporting pipelines and retail organization) located in El Dorado, KS by selling this property to a party who will operate it as a direct competitor with Texaco in that market. According to the FTC, the operation of this facility by a viable third party is a necessary prerequisite to their determination that the Texaco/Getty merger will not unduly upset the competitive balance in the affected market. What is troublesome to me is that it is unclear what the result will be if the El Dorado facility cannot be sold as a complete operating package within the 32 month period provided before, by the FTC. A distinct likelihood, I might add, according to several oil experts I have consulted in Kansas. Will Texaco be allowed to continue operating the refinery? Will the facility be closed down if a buyer is not found? What effect would either of these options have on the competitive balance in the area? It seems to this Senator that the effect of these possible scenarios should be addressed and addressed now.

COMMENT PERIOD

It is my understanding that the comment period regarding the Commissions tentative approval of this merger and the time for final approval will pass well before we find out if the El Dorado refinery can in fact be sold. The Texaco/Getty assets will be so commingled that even if we find out later the FTC plan for maintaining a competitive atmosphere in that market will not come to fruition it will be too late to do anything about it.

Mr. Chairman, I offer these detalis about the Texaco/Getty merger and the effects it may have on my State, its workers and consumers, to highlight my concern that full and complete analyses of these mergers be completed, commented on and reviewed before a final stamp of approval is given for any merger. The Texaco/Getty merger will have a profound effect on the citizens of my State, both in regard to the 1,000 jobs in El Dorado, KS that hang in the balance as well as the consumers across the State that rely on the availability of affordable petrolem products. I urge that diligent consideration be given to these serious issues.

A larger question that is posed concerns the need for oil exploration in this country and elsewhere. Over the past 25 years, we have seen fluctuations in both the demand and supply of oil, often accompanied by severe price disruptions. Large price increases have slowed consumption and served as an incentive to oil exploration. Current estimates vary, but it seems the best that can be said is that we don't truly know what our future energy needs will be.

We all recognize that in relative terms the U.S. has been thoroughly explored for petroleum. Despite all this production, proved U.S. oil reserves fell from 39 billion barrels in 1971 to approximately 28 billion in 1983. So it seems we ought to be be concerned about future supply, and that we ought to be careful about embracing a policy that serves as a deterrent to future energy exploration. If Texaco can, for example, increase its reserves from 1.05 billion barrels to some 2.3 billion barrels, they may have no incentive to engage in further exploration. Perhaps the FTC and the Justice Department ought to carefully consider the post merger exploration program of a company before consenting to a merger. It seems that at least we ought to take a close look at situations where an acquiring company assumes an enormous proportion of debt, the servicing of which necessarily deters oil exploration.

Mr. Chairman, I again thank you and the Committee for this opportunity to speak. I will review with interest testimony offered here today as I continue to formulate my position in regard to these issues.

HEARING RESUMES

The CHAIRMAN. We will be in order.

Senator, do you want to deliver your statement from the manuscript or do you want that put in the record in full and then you can summarize it?

Senator JOHNSTON. I would like to put my statement in the record, Mr. Chairman, and then summarize it.

The CHAIRMAN. Without objection, your entire statement will be put in the record, and we will now be glad to hear from you. After any of you Senators testify, if you wish to come up here and join us, you are welcome to do so.

STATEMENT OF A PANEL CONSISTING OF HON. J. BENNETT JOHNSTON, A U.S. SENATOR FROM THE STATE OF LOUISIANA; HON. DON NICKLES, A U.S. SENATOR FROM THE STATE OF OKLAHOMA; AND HON. WARREN RUDMAN, A U.S. SENATOR FROM THE STATE OF NEW HAMPSHIRE

Senator JOHNSTON. Mr. Chairman, I also want to thank you for this opportunity to testify and timely testify. I know you moved the date of this hearing up. We appreciate that.

Mr. Chairman, I appear before you as a friend of the oil industry in spite of the fact that some of my friends in the oil industry might not understand my friendship at this particular point in time, but I am also a friend of free enterprise, of the invisible hand, a friend of business, and I have supported almost every one of those, in fact, every one of those litany of things that Senator Metzenbaum read in his statement, of things that the Congress did in order to get drilling and exploration, things like deregulation of oil, deregulation of gas, promotion of exploration on the Outer Continental Shelf, getting rid of regulation by the Federal Power Commission.

In almost every instance, in fact, in every instance, I have either been the principal sponsor or a principal cosponsor of bills to help the oil companies because I believe that they have been right in seeking to explore.

I think it is manifestly in the interest of this country, Mr. Chairman, to have more exploration, and that is what brings me here today, because the present trend will inhibit rather than promote exploration both on the Outer Continental Shelf, and also onshore Louisiana.

Now, Mr. Chairman, I said I was a friend of free enterprise and the invisible hand, and indeed, when a number of years ago Shell Oil acquired Belridge Oil, I thought it was a good acquisition for Shell, and I did not at all disagree with that.

Then we began to get a trend but a gentle trend going, Mr. Chairman, in the last 3 years from 1980 to 1983. We saw United States Steel get Marathon. DuPont acquired Conoco. Occidental acquired Cities Service. A total of some $17 billion. Nevertheless, it was the invisible hand at work, I thought, and no reason for the Congress to protest.

But then, Mr. Chairman, what began as a gentle breeze a number of years ago and came into gale force winds in the last 3 years has now become a hurricane.

In the last 6 weeks, we see proposed another 29 billion dollars' worth of acquisitions and mergers. Texaco acquiring Getty for $10.1

billion. Socal and Gulf for $13.2 billion. Mobil acquiring Superior for $5.7 billion. As I say, that is $29 billion, and, Mr. Chairman, the Federal Reserve Board says there is only $497 billion of credit available to the country as a whole. Of that, this incredible size deficit that we have take up more than 56 percent of that, leaving only $216 billion total credit for everyone to build homes, to acquire automobiles, start new businesses and the three pending mergers now would take some 13.4 percent of all the credit available, those three mergers alone.

Mr. Chairman, if you are not frightened by those three mergers, then look at the list of the targets. Read it any day in the Wall Street Journal. Who is a proper target? I do not know, but what they talk about is Phillips at 12 billion dollars' worth of assets. Sun at $12 billion. Amerada Hess at $6 billion. Union of Cal at $8.5 billion. Kerr-McGee at $3.8 billion. Texas Eastern at $4.5 billion. Louisiana Land and Exploration at $1.7 billion. Freeport-MacMoran at $1.7 billion.

That is a total, Mr. Chairman, of 50.2 billion dollars' worth of assets in addition to the $29 billion now pending, and if that follows the same pattern as Texaco-Gulf where the price of the stock is written up over 100 percent in the process of this acquisition, you will have over half the available credit in this Nation, Mr. Chairman, used for acquisition of oil companies, not producing one new barrel of oil; in fact, working in absolutely the opposite direction.

It is no wonder that the eminent economist, Felix Roytan, says that it will make interest rates rise. I do not have to tell members of this committee what a rise in interest rates means, first, to the housing market, and then the automobile market, and then to the unemployment rate, and then you are into the same spiral of inflation, high interest rates, followed by recession.

It is not too much to say, Mr. Chairman, that this hurricane, this merger mania that we now have rocking Wall Street will, in fact, lead inexorably in that direction.

Now, just how are we going to finance, Mr. Chairman, these 29 billion dollars' worth of pending mergers and perhaps as much as another $100 billion of additional mergers unless stopped? Just how is it going to be financed?

Well, I will tell you how it is going to be financed. With tax deductible dollars. The taxpayer is going to finance these mergers. When Texaco goes out to acquire Getty, and they have already acquired them, and my bill does not affect that, but that $10.1 billion which has been borrowed will be tax deductible.

Now, to be sure, they will argue that there is a capital gains dividend to the taxpayer, and I am sure there will be a capital gains tax paid, but you and I know, Mr. Chairman, that a one-time capital gains tax paid at the low rates of capital gains is not nearly going to equal the raid on the taxpayers, on the Federal Treasury that the writing off of this debt service over the period of years will cost the taxpayer, will cost the deficit.

Mr. Chairman, that deficit is somewhere between $180 billion to $200 billion, depending on whose figures you believe. I have been working on a plan, I am sure you have, too, to reduce that deficit.

No easy, painless way. I mean, it involves doing things like cutting down on the rate of increase for defense or cutting back on school lunches. You know, we have cut back 3 million school lunches under this administration. I have supported some of those cutbacks.

But, Mr. Chairman, it hardly seems right to be taking billions of dollars for oil acquisitions financed by tax deductible raids and using that money for windfall profits, and I hate to use that word "windfall profits" because I thought it was misused when we talked about windfall profits on oil, but you can believe it is properly used here when one group can make as much as $780 million, one small group, on Gulf stock alone with no heavy lifting involved and all within a period of about 1 year. Now, that is what I call windfall profits, Mr. Chairman.

Now, what will the industry look like the day after? Well, it is not hard to tell. First of all, you will have fewer companies. We know that. They will be bigger companies. They will have bigger debts. Indeed, almost twice the debts.

Now, what are the implications of that, Mr. Chairman? You do not have to be a fancy economist to know what the implications of a bigger debt are. That means less money left over for everything else.

Even after Socal, which is a great company run by a great chairman, even after that company acquires Gulf and gets its tax write-off, it is going to have fewer dollars with which to explore.

I do not know what Gulf and Socal's budgets are going to be for exploration, but I can tell you they are going to be less. We have asked and have not been able to find out. I doubt if they have put them together.

But they cannot be as much. You simply cannot borrow $29 billion with three companies and have as much left over to do everything else. Mr. Chairman, I mean 2 and 2 just equals 4 in spite of what people say.

Now, if there are bigger debts, there is less for exploration; it will be as Felix Roytan says, inflationary. There will be higher interest rates because there is going to be less money to go around.

Now, just what happens to the money, Mr. Chairman? This seems to be a key question around here. The Wall Street Journal said the other day: "Well, the money stays in the system." Mr. Chairman, they are dead wrong.

Some of the money stays in the system, of course. But again, it is common sense. There is no additional wealth being created by these mergers, not one new barrel of oil, not one new dollar's worth of property being acquired. There is only additional incremental debt, and indeed, there are no new oil companies being created.

So what you do is you take the price of Gulf stock, write it up from $29 or $30 a year ago up to $80. The differential is going to be represented by debt. Then you are going to give money to those who held the stock, and I applaud them. I think Boone Pickens, if I may say, is one of the brightest, most creative, best examples of an entrepreneur in this country. If I was not in the Senate, I would be wanting to invest with him. I applaud him.

But should we set the rules of the road so that someone in his position can make $780 million financed by taxpayers beneficence? I do not think so, Mr. Chairman. That money does not get back in the system.

Some of that money will get back in the system. If you go to Las Vegas and you do some gambling and you win some money, yes, some of it might get back into oil exploration. Some of it may get back into another trip to Las Vegas. Some of it may get into buying a boat. Some of it may get into the stock market.

But when you buy stock of existing companies on the stock market, it creates no new issue, no new entrepeneurial opportunity, no new business. It is simply more money in the same hands to do the same things.

Now, finally, Mr. Chairman, let me say that domestic exploration is a serious problem in this country. Domestic reserves are down 17 percent in 10 years. Domestic imports are creeping up again. Domestic production is creeping down again. Domestic use of oil, consumption of oil is going up.

We estimate that 59 percent of future crude oil must be offshore; 39 percent of future natural gas must be offshore. These investments offshore, by and large, Mr. Chairman, must be done by the major companies.

What we are doing here is creating fewer major companies, more burdened with debt, less able to explore in those areas which will produce most of the oil and gas in this country if it is found.

Finally, to those who say we must delay, I can say that delay will only defeat this measure. If you are for reaping the hurricane or the whirlwind or if you are for what may turn out to be as much as $100 billion of additional debt financed by the taxpayers, then, indeed, you are for delay.

I think the Congress ought to address itself to the question and do so promptly. What is the solution? What happens at the end of 6 months? Well, Mr. Chairman, I would say at the end of 6 months what the Congress should consider at that time is, first of all, whether it is in the national interest for this to happen. Second, whether the taxpayers and to what extent the taxpayers ought to underwrite these kinds of acquisitions, and indeed, that kind of legislation is presently before the committee.

We ought to consider whether or not the royalty trust, which is a form of liquidation of oil companies, whether that is in the interest of the Nation or, to put it another way, whether distributions out of that royalty trust ought to be accorded favorable tax treatment or whether they should not.

These are monumental questions, Mr. Chairman, affecting the very nature of the oil business and also affecting the purse of this country.

I believe that this bill, which, for a period of 6 months would prevent the top 50 companies—that is, those with worldwide reserves of 100 million barrels a day—prevent anyone from acquiring those 50 companies.

It would also prevent anyone with a royalty trust or affiliated with a royalty trust now or in the past to acquire or solicit a proxy for more than 5 percent of the top 50 companies, and if they do so after February 28, which is the date which does not affect Texaco-

Getty but does affect those mergers after that time, then it would provide that they must divest within a period of 30 days.

Mr. Chairman, I believe this is a reasonable approach. It will give the Congress time to work its will on these great questions, and I hope that the committee will examine this matter and report favorably on this bill.

6-MONTH MERGER MORATORIUM

The CHAIRMAN. Thank you very much, Senator.

Senator Johnston, the prepared statements of several oil company representatives express concern over the possible retroactive application of any merger moratorium. You have noted your intention to exempt the Texaco-Getty merger because the Federal Trade Commission has already given preliminary approval and the stock has changed hands, I believe.

If, at the time the Congress were to pass moratorium legislation and if other mergers were in a similar procedural situation, what would be your position?

Senator JOHNSTON. Mr. Chairman, this legislation that we will propose will not affect, as I say, Texaco-Getty, but it will affect all those that come after February 28 which was the date upon which the legislation was first offered, and at that time, we served notice that all mergers after that time would be subject to this 6-month moratorium. So it would affect all of those after February 28.

The CHAIRMAN. In other words, the Texaco-Getty merger would be the only one that would be exempt under your legislation?

Senator JOHNSTON. That is correct, Mr. Chairman.

The CHAIRMAN. Senator Johnston, you have expressed concern over the effect of large oil mergers on exploration activity, I believe.

In his submitted statement, Mr. Keller has noted that Socal intends to continue its exploratory program comparable in effort to the total of the programs Socal and Gulf would have done individually. How would you respond to this statement by Mr. Keller?

Senator JOHNSTON. Mr. Chairman, I am sure he said that, and if he said it, I am sure he means it. However, I would say it will be impossible or very difficult for any merged company which is saddled with $13.2 billion in new debt where the cash flow must first be used to retire that debt to explore as much as they did before.

We have asked for the figures for the next 3 years from both Gulf and Socal as to what their exploration program is, and I have not gotten those yet, although we have asked for them. Maybe they are not confected yet.

But I can tell you that there is no way. It does not make sense, Mr. Chairman, that companies can merge and be burdened with all this debt by writing up the stock at twice its value and end up exploring more.

[Prepared statement follow:]

Statement of Senator Johnston

Mr. Chairman and members of the Committee, I am pleased to appear before you today to discuss the matter of mergers in the oil industry. I believe that by holding this hearing you have further demonstrated your ongoing commitment to give serious attention to this most important matter.

As you know, I have sponsored legislation which would operate to restrict oil company mergers for a brief period of time to facilitate further review. My legislation provides for a six-month moratorium on mergers of the companies holding the largest oil and gas reserves (over 100 million barrels equivalent of oil and gas - the top 50 companies). It also prohibits any person with an interest in a royalty trust from acquiring a total of more than five percent of the voting stock of any of these companies, or from soliciting proxies from other stock holders of these companies. A special commission on mergers, similar to the Linowes Commission on coal leasing practices, would be established. This commission would receive input from the Departments of Justice, Treasury, Interior and Energy, and the Federal Trade Commission as to the impact of the mergers.

I offered this legislation because I believe the recent spate of mergers in this industry has profound implications for the future. If, as some have argued, the oil industry is undergoing a transformation, then I believe we in Congress have a duty to review the implications of that transition. Many have asked "why single out the oil industry for such a review?" The answer to that question is two-fold, and contains the thrust of my concerns.

The first reason for singling out the oil industry is because of the enormous size of the mergers about which we are talking. In the last few weeks, we have witnessed a $10.1 billion takeover of Getty by Texaco, a $13.2 billion offer for Gulf by SoCal, and a $5.7 billion offer for Superior by Mobil. This is $29 billion worth of borrowing in a few short weeks. The asset values of other oil companies who are potential takeover targets total over $100 billion.

I believe we must assess what implications this type of borrowing has on the credit markets of this nation. According to Federal Reserve Board analysis included in the President's budget there was $497 billion of credit flow in domestic capital markets in 1983. Federal borrowing needs, including the Federal deficit, totalled $281 billion, or 56% of the total credit available. This left $216 billion available for private borrowing. Had the Texaco, SoCal and Mobil mergers occurred last year they would have consumed almost 14% of all capital available for private purposes. Purchases of other potential targets could eat up half of the available credit.

If, as economists tell us, the unacceptably high level of Federal borrowing puts upward pressure on interest rates, thus threatening economic recovery, then I contend that borrowings for purposes of acquisition have the same effect. And, as if to add insult to injury, the interest payments on these huge loans are tax deductible, meaning that the same small borrower who may be crowded out of the capital market is effectively subsidizing mergers between giant oil companies.

Many of our recent economic policies have been designed to lower interest rates and facilitate borrowing. But the purpose of so doing was to encourage new capital investment of the sort that expands employment and stimulates economic growth. Acquisitions of large oil companies have no such consequences, and indeed through consolidation may result in a reduction of jobs in an industry already hard hit by the recession.

I know that certain of the witnesses who will follow me will contend that this money does not disappear--it remains in the system. Indeed this is so. But like monies lost at the gaming tables at Las Vegas, we are uncertain as to the uses to which it will be put. Much of it will undoubtedy remain within the stock market itself, expanding the pool of money that investors are able to exchange amoung themselves. However, these intra-Wall Street transfers of existing securities do little to stimulate <u>new</u> capital investment such as we are seeking. Even assuming for purposes of

argument that these monies are put into new capital investment, undoubtedly only a fraction will find their way back into the oil exploration industry.

This brings me to my second point--the effect of these giant mergers on future exploration activities of the oil companies involved. A $13 billion merger between two oil companies does nothing to expand either the combined asset base or the earning capacity of these companies over what it would be if they remained separate. Yet it does serve to dramatically increase the debt load of both. By borrowing $12.5 billion to acquire Gulf, SoCal's debt share would rise from 7% of total capitalization--the lowest among major oil companies--to 40%, among the highest.

This increased debt must be serviced and liquidated with revenues generated from the existing asset base. It is my concern that these revenues will be those that would otherwise go to exploration for new oil and gas. The possibility that exploration monies will go for debt service increases dramatically if either interest rates rise or oil prices fall.

Again, I know that subsequent witnesses will tell you that the exploration budgets of the merged companies will remain constant and will increase in efficiency. But let us take a look at what the exploration program of Cities Service has done since its acquisition by Occidental. Acording to Solomon Brothers, Cities' exploration budget declined from $843 million in 1981 to $310 million in 1983--a reduction of more than 63%.

I have asked Socal and Gulf about their exploration and production plans. From 1978 to 1982, Gulf spent $2.1 billion on exploration and production, while Socal spent nearly $3 billion. Gulf projected it would spend $7.5 billion from 1984-1988. Socal has not provided me with its projections. But based upon recent experience with other mergers, I frankly doubt that the combined budget would be as vigorous as it would have been.

In the ten years since the Arab oil embargo, ours was the only major producing nation whose production levels went down. Indeed, our domestic oil reserves declined by an alarming 17%. I am deeply

concerned that should the merger trend continue that the result will be less domestic exploration and a further depletion of domestic reserves, leading to more oil imports, an increased trade deficit, and greater vulnerability to the political uncertainty of the Middle East.

Mr. Chairman, I have never subscribed to the theory that big necessarily means bad. However, I do fear that some methods of getting big may have bad consequences. This is my concern with the recent wave of mergers, and this is why I believe Congress has a duty to review the implications of these mergers.

Before I conclude, let me say a word about royalty trusts. With all due respect to my friend Boone Pickens, for whom I have a deep and sincere admiration, I believe the royalty trust concept is an anathema to the oil industry of this nation.

American industry is frequently criticized in the world market for not following long-range, forward thinking corporate strategies. It is argued that American business pays too much attention to this quarter's profit margin and next quarter's dividend. Many note that our world competitors, such as the Japanese, tend to sacrifice short term profits for higher long-term market shares.

This criticism of American industry can be debated insofar as many industries are concerned, but I think it unquestionably does not apply to oil companies, particularly insofar as exploration activities are concerned. The vital role which crude oil and natural gas play in our economy, and the factor of dwindling domestic supplies, have forced our nation's oil industry to undertake long-range, advance planning for future exploration.

Estimates are that 59% of future crude oil discoveries and 39% of future natural gas discoveries will be made offshore. Many of these discoveries will be made in remote areas such as offshore Alaska and the North Sea. It generally takes 5-7 years to bring oil on stream from such discoveries. Operations to do so require the type of long-term planning, financial commitments and technical expertise not frequently found nor haphazardly assembled.

I deeply fear that the royalty trust concept poses a grave danger to the type of exploration activities that this country deeply needs. By taking advantage of the general undervaluation of oil company stock prices, the royalty trust threatens to mortgage our long-term exploration capabilities for the short-term benefit of stockholders. This is the type of bottom line profit motive that future generations of Americans can scarcely afford to tolerate.

I believe this nation has generally been well served by our oil companies, big and small. That industry may well be undergoing a transformation. But if that transformation must be accomplished through wholesale mergers, then I believe we in Congress should review the implications of that trend. The industry can afford to wait six months--we cannot afford not to.

The CHAIRMAN. Thank you very much.

The distinguished Senator from Utah.

Senator HATCH. Thank you, Mr. Chairman.

Senator Johnston, it is my understanding that substantial competition now exists in the domestic oil and gas industry.

Senator JOHNSTON. I would agree with that.

Senator HATCH. Experts tell me that by any standard from reserves to production to marketing, the oil industry is unconcentrated. Do you agree with that as well?

Senator JOHNSTON. Yes, I would agree with that.

Senator HATCH. I think we are here today to examine really some of the competitive aspects of your particular amendment. I might add in none of these categories that I have mentioned does the top 10 firms control even 50 percent of the production or sales, and I think you understand that to be true as well.

Senator JOHNSTON. Yes, I would certainly agree with that.

Senator HATCH. The domestic oil industry faces intense competition from foreign governments and foreign competitors. Do you agree with that?

Senator JOHNSTON. Well, I would not put it like that, not in terms of——

Senator HATCH. Well, let me say foreign companies, then.

Senator JOHNSTON. Would you include Shell in that category, BP?

Senator HATCH. Sure.

Senator JOHNSTON. Well, Shell would not consider itself foreign, certainly not Shell USA, and BP, well, I will let them debate whether they are foreign or domestic.

Senator HATCH. But there is intense competition internationally. I think that is basically what I am asking.

Senator JOHNSTON. Well, I think the oil industry is one of the crowning glories of this country. I think our technology, our know-

how, our companies are the best in the world. That is why we discover most of the oil in the world.

I mean, we are not competing, for example, with Saudi Arabia in the sense that they might do it better than we. Our only competition might be that how much of the oil we discover they let us take. That is what the competition is. We lead the world.

Senator HATCH. Is there something, in your opinion, wrong with the present Hart-Scott-Rodino act and other Federal antitrust laws that would justify the adoption of the type of extraordinary legislation that your amendment represents here?

Senator JOHNSTON. I am not ready, at this point, to suggest a change in antitrust laws that might come at the end of 6 months. It may be that we will examine this trend and say that fewer bigger companies burdened with debt are somehow more efficient, somehow in the interest of the taxpayer, somehow in the interest of exploration.

I do not think we will find that. If we find, as I suggest, that it is a great cost to the taxpayer, less competitive, more unwieldy, with less of an exploration budget, I am not sure precisely what the antidote for that is.

It may be tax legislation to say that if you make a preditory acquisition, you are not entitled to have that acquisition underwritten by the taxpayers in terms of a deduction from your income tax return for the interest.

Senator HATCH. Well, it may be that we need to let the appropriate committees of the Congress really look into this, because I share some of the concerns you do.

Senator JOHNSTON. I know, but after all of that has taken place, and has taken place under today's rules, then what are you going to do? Are you going to say to Socal, "Well, sorry, you made that acquisition based upon that, and now we are going to deny you the tax deduction"?

Senator HATCH. Well, if, at the end of the hearing process, your position is meritorious, and it may very well be, I'll join you in your position. For instance, today, we have this hearing. Wednesday, March 21, the House Energy Committee and Subcommittee on Fossil and Synthetic Fuels and the Subcommittee on Commerce, Transportation and Tourism is going to hold a hearing.

On Friday, the 23d, House Judiciary Committee, the Subcommittee on Monopolies and Commercial Law will hold a hearing. On Wednesday, March 28, there will be joint hearings between the House Energy Subcommittee and Telecommunications, Consumer Protection and Finance and the Senate Banking Subcommittee on Securities, and then finally on April 10, Tuesday, there will be a Senate Energy Committee, Subcommittee on Energy and Mineral Resources.

So I am concerned about the process working.

Senator JOHNSTON. Well, I am concerned about it, too, and I am concerned about it working within any timeframe in which to allow for any legislation to go through. If we waited for all those committees to report or even for the principal committee to report, we would not get any legislation this year.

I have been trying to pass coal slurry pipeline legislation here for a number of years. I got caught last year in in the closing hours. I

got caght in the previous Congress, and have not had the opportunity to bring it up because I was told to wait until the hearing process is finished.

Now, if you want all the mergers to go through and let it be too late to do anything about it, then I would say, sure, let the committees work their will, and let the floor work its will, and somebody will be out there filibustering, and we will be saying too bad on the last day of the session.

Senator HATCH. Let me ask you a couple of questions on the effect of your amendment. What effect do you believe your amendment will have on the future of the two types of oil companies created by this amendment, the super large and everyone else? Do you think it will have any real effect?

Senator JOHNSTON. Well, what the amendment would do, it would prevent the merger of any of the top 50, that is 100 million barrels of worldwide reserves. It would also prevent anyone who has an interest or has had or is an affiliate of a royalty trust or is acting in concert with any such person to acquire as much as 5 percent of any of these companies.

So it is designed to stop all the mergers, all the mergers of the big companies, acquisition of control during this period of 6 months.

Senator HATCH. Except that a number of large mergers have already occurred.

Senator JOHNSTON. Yes. There is a basic principle of fairness involved, and it is always a difficult call. I thought the proper call was to say that anyone who is not on notice, namely, Texaco, Getty, Marathon, Cities Service, all of that, that litany I just read, they made their deals before we introduced our legislation. They were not on notice. Everyone after February 28 was on notice.

Senator HATCH. What effect do you think your amendment would have on other corporations outside of the oil and gas business? Would they be able to buy into the oil and gas business?

Senator JOHNSTON. Not with one of the top 50 during this period of 6 months.

Senator HATCH. What would happen if your amendment passes, and I have some idea of what might happen, but I would like to hear what you think. What would happen if your amendment passes to the perhaps thousands, maybe tens of thousands of institutional and individual shareholders and pension plans that are holding the effected shares?

Senator JOHNSTON. What happens in what timeframe?

Senator HATCH. Well, if your amendment passes, during that 6-month timeframe of your amendment and thereafter. I think that is an important question because, see, it is not just two big companies merging. There are thousands of shareholders involved who may or may not benefit from these mergers. Only time will tell. There are all kinds of other intricacies and questions that have to be asked. It is not just a simple "big is bad" with a company merging.

Senator JOHNSTON. There are also millions of taxpayers who are going to underwrite these mergers and the windfall profits that go with them. So what you are asking, I guess, is what would the price of Gulf stock be on the day after this legislation passed.

Senator HATCH. No, I am not really asking that. I am saying that is part of it. I am asking that you have about 65 million shares held long-term by various individuals and about 36 8 million short-term in the Socal-Gulf merger.

Senator JOHNSTON. Well, what would happen depends upon the date upon which the legislation was passed. If the legislation was passed today, then a solicitation by Mr. Pickens would be delayed or stopped, should I say, on Gulf stock. That is at $65. The proposed solicitation by Socal, which has not yet cleared the FTC, would also be delayed. I cannot tell you exact what the price of Gulf stock would be. That is a function of the market.

Senator HATCH. What if Socal clears the FTC before the moratorium expires? What happens then? Or before your bill passes even, to put it in another form?

Senator JOHNSTON. Let us say we do as you suggest and wait for the committees work their will and legislation——

Senator HATCH. Well, we have present laws that are supposed to take care of these very problems that you are concerned about, and I have never thought those laws to be inadequate or capable of solving these problems, but perhaps I am wrong. That is why I am asking these questions.

You have all kinds of individual investors who are involved who would tend to benefit from this transaction, just using the Socal-Gulf situation.

Senator JOHNSTON. Let me tell you this, Senator Hatch. I can tell you this. There would not be one barrel of oil lost for Gulf. No asset that Gulf now holds would be worth less as a result of this legislation passing other than whatever speculative effect various mergers would have. Intrinsically you would still have the same value. So you lost nothing with respect to that.

Senator HATCH. You may still be right. But I think you would have a rough time selling that to the stockholders who were involved in this matter. For instance, as I understand it, from this one merger the Federal Treasury stands to gain from individual shareholders in taxes. They will be taxed on their gains in this matter from the corporate investors something like $2 billion if that transaction goes through.

Senator JOHNSTON. I do not know what the amount is. I know that long-term capital gains rates would not be that much. Maybe there is some short term on it.

Senator HATCH. Well, the MESA group would have a tax rate of 46 percent. They would be taxed somewhere in the neighborhood of $350 million.

Senator JOHNSTON. Well, I do not know whether that is long term or short term.

Senator HATCH. The corporate spectulator would be taxed at 46 percent, too, and they would have $251 million, as I understand it, tax cost. Institutions, about $154 million. Individuals, around $780 million, long-term individuals and short-term individuals, about $460 million. Which would come to almost $2 billion—$1.995 billion.

Senator JOHNSTON. I do not know. I cannot disprove that at all. I do not know whether that was short term or long term. If it is long-term rates, it would certainly be less than that. If it is short term

rates, that may be in the ballpark. I do not dispute that. I would dispute the fact that that would exceed the writeoff of the interest on a debt of $13.2 billion.

Senator HATCH. What effect would your amendment have on the ability of the frozen oil companies to compete during the moratorium and even afterward? Would it freeze them and make it even more difficult for them to compete or do you take the position that they got themselves into this and they are going to have to worry about getting themselves out of it?

Senator JOHNSTON. No; it doesn't affect at all the ability of an oil company to explore, to do the things that are productive; indeed, they say they are continuing to do that now.

As a matter of fact, the point you make is a valid one in this sense, and that is as long as oil companies are takers or takees, and they are all fair game now—I mean, even after Texaco made its acquisition, it thought it had enough shark repellant, but then along come the Bass brothers and they found that they were in jeopardy, so they had to pay $5 over the market in order to acquire that stock from Bass brothers. The top management, I can tell you, in these companies is spending more time worrying about whether they are going to be a taker or a takee than they are on putting together exploration budgets. I can also say some of them are worried about this legislation right now.

But the fact of the matter is that this merger mania is occupying the time and attention and certainly the dollars of major oil companies today.

Senator HATCH. What about the problem that Gulf has? If your amendment passes, how will it prevent its own liquidation through various proxy fights and other competitive fights during this moratorium period? Would not that be a serious loss to the——

Senator JOHNSTON. No; it would prevent proxy solicitation during this time. It would not, of course, prevent the shareholders, at an annual meeting, from electing whoever they wished as management, but it would prevent proxy fights and acquisitions, or mergers, during this period of time.

Senator HATCH. My time has expired. I will be happy to come back.

[Prepared statement of Senator Orrin G. Hatch follows:]

OPENING STATEMENT OF SENATOR ORRIN HATCH

Mr. Chairman, I want to thank you for scheduling this hearing concerning the current merger activities in the Nation.

As we are all aware, since the first of the year several major transactions have occurred in the oil industry, including the merger of Texaco and Getty, the merger of Socal and Gulf and now Mobil's acquisition of Superior. One major oil company has averaged a $12 billion line of credit and several smaller energy companies are engaged in acquisition attempts. In addition, the Justice Department recently rejected a proposed merger between two of the Nation's steel companies. During 1983, several of our major railroad companies were also involved in major acquisitions, mergers and consolidations. Additional major transactions in the railroad industry are rumored to be in the offing.

Mr. Chairman, the pace and numbers of major corporate acquisitions have raised concerns and questions among many of our colleagues. I, too, have questions about some of these transactions. I share the concern of all of my colleagues that these transactions and other activities in the marketplace result in greater efficiency, a strengthened economy for our nation and better prices and service for the American consumer.

On February 29, during our consideration of the Export Administration Act legislation, our colleagues, Senators Metzenbaum and Johnston, offered amendments that would prohibit many of the recent oil company mergers and acquisitions and would provide a six month moratorium on future oil company mergers and acquisitions. Both of these amendments were defeated, but by sufficiently close votes that the issue of antimerger legislation is very much a current topic of discussion in the Senate.

I would hope, Mr. Chairman, that the Senate will not act precipitously in this area. Before acting, we should at least understand the facts, the public policy considerations and the full impact of any proposed legislation. The hearing today should give us a good beginning in our quest for such understanding.

The CHAIRMAN. The distinguished Senator from Ohio.

Senator METZENBAUM. Senator Johnston, following up on your exchange with Senator Hatch, is it not the fact that if we don't do something immediately and not follow the laborious process of legislation, that all the horses, or many of the horses, will be out the door and it will be impossible to put them back? In other words, we either must act promptly or the mergers will become accomplished facts, and, just like Texaco-Getty, it's really too late to do anything about it?

Senator JOHNSTON. That is exactly right. If we don't act and act pretty quickly, then at some point even I would join with those, as I have on Texaco, and say it is just too late with Texaco—and at some point that happens with Socal-Gulf and with Mobil.

It is not there yet, but at some point it would be there.

Senator METZENBAUM. And at this point, neither Socal-Gulf nor Mobil-Superior are consummated—offers have been made, but the shares have not been exchanged; and if Congress is to act, we must do it very promptly

Senator JOHNSTON. I think we must, virtually immediately—I would say certainly within the next couple of weeks, I think

Senator METZENBAUM. And when my distinguished colleague from Utah is talking about all of the revenue we are going to receive as far as taxes are concerned, isn't it also the fact that it is pretty speculative to decide how much those tax revenues will be because so many of the shares are held by tax-exempt pension funds and other considerations over and beyond that?

Senator JOHNSTON. That is exactly right. And, again, you don't know whether it's long-term or short-term gains.

Senator METZENBAUM. You don't know whether they have shelter, the people that——

Senator JOHNSTON. I would imagine most of the people in this bracket would have shelters.

So I think it would be highly speculative to say what the tax would be.

I would be willing to bet that it would be much less than is going to be raided from the Treasury in terms of interest write off over the period of time.

Senator METZENBAUM. I thank you. Thank you, Mr. Chairman.

Senator HATCH. My understanding, if the Senator would yield for 1 second, is that the tax-exempt number of shares is about 10 million shares out of a total of 165.3 million

Senator METZENBAUM. I might say that I am sure that the distinguished Senator from Utah doesn't really claim that we ought to permit this merger because it might possibly result in some tax

revenue when we know, as the Senator from Louisiana has already pointed out, on $13 billion of borrowing at 10 percent, that will cost $650 million a year just as far as taxes are concerned in deductions for the interest alone.

Senator HATCH. Well, I am not arguing that; I just wanted to bring those points out.

The CHAIRMAN. The distinguished Senator from Pennsylvania.

Senator SPECTER. Thank you, Mr. Chairman. Senator Johnston, regarding predatory acquisitions not receiving any tax benefits, and combining that with your comment about how long it takes to get anything done on Capitol Hill, don't we already know enough to begin to make a movement against predatory acquisitions and not to give them the benefit of the tax breaks if we can define a predatory acquisition?

Senator JOHNSTON. I think so. I don't know how long it takes the Finance Committee and the House Ways and Means Committee to act and how long it takes to get that legislation up on the floor, but my point is that unless you pass some moratorium like this very quickly, then you are going to have many of these acquisitions made in reliance upon present tax policy.

And that brings up that fairness argument. I mean, there are some who would say, for example, that Socal-Gulf is not a good deal. I have heard one oil company president say he looked at it and didn't like it; he thought it was too marginal. I got a lot of confidence in Mr. Keller, but I am sure Mr. Keller and his group relied upon present tax policy, and if you didn't have that interest write off, my guess is he might want to reconsider.

Senator SPECTER. Well, the Finance Committee is pretty well advanced along the line of modifying the dividends-received credit, and there has been a lot of consideration given to eliminating the interest deduction on a predatory acquisition, just as the interest deduction cannot be taken when acquiring tax-free bonds. There has also been a lot of consideration to limit an acquiring corporation's declaration of a short-term capital loss when the acquired stock is sold after royalty trust interests have been distributed.

If we were to enact those three aspects of tax reform, wouldn't we stifle the so-called predatory acquisitions?

Senator JOHNSTON. I think that would go a very long way. I think it would be very difficult to make these predatory acquisitions without favorable tax treatment. I am not a tax expert, and I can't tell you what the dollars involved are—my guess is it would knock that in the head.

But again the question is what do you do for those that have already taken place? What do you do, for example, for Shell-Bellridge [?], which took place I think in 1978, was it?—some time ago, in any event. I don't know whether they had debt, but if they did it seems to me they did so in reliance upon present tax policy before anybody criticized that. You would have a strong fairness issue there.

So I say don't let the mergers go through now, so that you can examine those without having that fairness issue that comes in and say, well, gosh, we did all this in reliance upon tax policy, and, if you put this in, you will bankrupt the second greatest oil company in the world.

Senator SPECTER. Well, as to the acquisitions which are already completed, there would be no effort necessarily to unscramble the eggs, but why couldn't we deal with those tax issues which we know the answer to as a more effective way of dealing with the problem than a 6-month moratorium?

Senator JOHNSTON. Well, the 6-month moratorium is in aid of what you are saying. You ought to stop and let the Congress take a look at it during that period, to look at tax policy as well as look at antitrust policy and energy policy.

Senator SPECTER. Senator Johnston, what would you think about modifying the takeover laws as to the SEC aspect? The Securities and Exchange Advisory Committee has recommended that the law be amended to require that any person or corporation seeking to acquire more than 20 percent of a class of equity stock in a corporation be required to make a tender offer to acquire all the shares of that equity class.

Now, that would not preclude some mergers where most or all the stock is acquired, but don't you think that would be a significant step in the right direction, by precluding some of the predatory takeovers where there is not enough financial ability to acquire all the stock?

Senator JOHNSTON. I don't know whether that would preclude the predatory takeovers; it would certainly be a good fairness issue, because if there is to be a predatory takeover, it ought to be of all the stock.

Now, to what extent it would prevent predatory takeovers, I don't know.

Senator SPECTER. Senator Johnston, what would your view be about amending the standards that the FTC uses to evaluate mergers, to take into consideration the acquisition of foreign ownership of assets which were previously domestically held?

Senator JOHNSTON. Well, I think it ought to be evaluated; I don't have a judgment on that now. I am not an FTC expert.

I know this much: If FTC would let Texaco-Getty go through, with only one dissenting vote, my guess is that anything will go through the FTC—oh, with a complementary divestiture here and there of a few gas stations and a little marketing and maybe a little refining. But I don't think FTC right now is any effective break upon merger mania.

Senator SPECTER. Well, one approach might be to amend the FTC laws and to give them different standards to apply; and another standard which has been suggested would be to consider the tying up of large amounts of otherwise available credit; given the high interest rates and the very heavy Federal borrowing, which we are trying to do something about, it is hardly in the interests of public policy to have somebody going out into the credit market and tying up $15 billion.

Wouldn't that be an appropriate factor for the FTC to consider?

Senator JOHNSTON. I think it exactly would, and it is a very appropriate thing for the Congress to consider at this point.

I think you came in right after I had been talking about that issue, and the amount of Federal credit that is being sopped up by these mergers. The $29 billion now pending constitutes, according

to the Federal Reserve Board, 13.4 percent of the total available credit. That is just those presently pending.

And then if you take all of those mentioned as targets at their present, which is $50.2 billion, and say you are going to write up that stock by 50 percent, as you did in Texaco, you have got over 50 percent of the available credit. That is a very powerful issue

Senator SPECTER. Senator Johnston, I would like to explore one other subject with you briefly because we are keeping Senator Nickles and Senator Rudman waiting, and that is the subject of the Gulf-Socal situation, which would not be excluded under your legislation. That is of particular concern to a Pennsylvania Senator, although the overall problem is a concern of every Senator.

I have had discussions with the leaders of those companies and have frankly stated that I am not favorably disposed to the merger unless it proves to be the least of the undesirable alternatives, which it may well prove to be. Gulf did not seek the merger until they were threatened by an acquisition from Mr. Pickens and Mesa.

Perhaps indelicate, but do you think that the Pickens-Mesa effort to acquire Gulf was a predatory acquisition effort?

Senator JOHNSTON. Well, that is a pejorative word, and——

Senator SPECTER. Well, I didn't start the word or the effort.

Senator JOHNSTON. If your interest is the survival of Gulf as an ongoing oil company, able to go out on the Outer Continental Shelf, able to produce energy for the company, then decidedly it is not good.

If your interest is instant gratification for the stockholder, write up the value of the stock immediately, it clearly is.

I think the value of that stock will move up in any event, whether by the Pickens tender, by Socal, by some other tender, or by the action of the market, because the reason the stock was down is because—I mean, the reason it was able to go up was because the assets in place were worth a lot more. And I think people understand that now, and I think management of Gulf, frankly, had become very aggressive in recent months; I think they had gotten rid of something like 14,000 employees, were in the process of streamlining their company, making it more, as someone said, lean and mean; and they had an active exploration budget of I think a couple of billion dollars, as I recall.

I think Gulf was going to make it anyway; they didn't have time; they just didn't have time. But the value of that stock will eventually be reflected, whether in the instant tender presently pending—Socal tender—or by the action of the market later.

Senator SPECTER. Well, Senator Johnston, as you have defined, keeping Gulf in existence on the outer shelf, on the one hand, or looking for instant gratification of shareholders resulting from having more money for their stock—the latter is what happens as a result of the effort by Mr. Pickens and Mesa—I would say that it would qualify for being a predatory acquisition effort, pure and simple; that is what it is. It seems to me we ought to be looking now for specifics on ways to deal with that kind of a problem, because after Socal acquires Gulf, if it does, Mr. Pickens and Mesa are likely to try to acquire Socal.

We haven't seen the end of it. Unless we deal with the dividends received credit, and the capital gains juggling, and the interest deductions, we are going to be right back here for 6 months, and 6 months, and 6 months.

Senator JOHNSTON. That's right. There is no more end to this—I mean, Texaco may have thought that they were immune, and then along comes the Bass brothers. The Bass brothers say they had no such thing in mind—and I don't dispute them. But Texaco thought they might be, otherwise they wouldn't have paid $5 over the market to purchase their stock.

No one, it seems to me, is fully immune. And, you know, they talk about shark repellent—how do you get yourself into a position where nobody can take you over? Well, one of the biggest ways you do is you burden yourself with so much debt that you are no longer desirable—and that is certainly not in the interest of the United States, to burden all our big oil companies with so much debt that they are no longer desirable. Because, look, if these interest rates go up or if the price of oil goes down—and both of those things have been predicted to happen, I hope they don't—then all of these merged companies are going to be in some difficulty.

Senator SPECTER. Well, it seems to me that—I have been around here enough 6-month periods to know that not much happens in the Congress in 6 months, we really ought to be——

Senator JOHNSTON. A lot of people here would say too much.

Senator HATCH. That all depends.

Senator SPECTER. We really ought to deal with the underlying problems. I have grave concern about seeing Socal merge with Gulf because it has already been declared that the Gulf headquarters in Pittsburgh will go and perhaps as many as 900 jobs will be lost. We are going to have to consider that to determine the consequences. There are also major Gulf interests in the other end of the State, in Philadelphia.

I don't like a situation where Gulf has to go to Socal for a white knight. We really ought to construct the laws so that we allow mergers and allow acquisitions where they have a legitimate purpose for public policy, but not where they are predatory.

My instinct is to try to tackle the problem now and try to come to some answer to it.

Senator JOHNSTON. I am completely in agreement with you. I think I am completely in agreement with you.

Senator SPECTER. I thank you very much for your testimony, Senator.

Thank you, Mr. Chairman.

The CHAIRMAN. The distinguished Senator from Utah.

Senator HATCH. I don't mean to keep you much longer, but I am concerned because—you and I chatted just a day or so ago, and you indicated to me that you feel very deeply about this, and I do, too—I am not sure which is the best way to go, but I am concerned that what you are doing may in essence hurt an awful lot of people or may help a lot of people; it depends upon what position you are in.

But my reading of your amendment is that it may inhibit economic growth—we have brought out the potential for its effects on Federal tax revenues. It also could penalize private pension funds.

And I brought out that of the 165.3 million shares involved in this transaction, there are only 10 million that are tax exempt.

Senator METZENBAUM. How do they know that?

Senator HATCH. That is what I have been informed is the case.

Senator METZENBAUM. So many shares are held in street name at the broker's office. How do they know how many are owned by pensions?

Senator HATCH. Well, I can't answer that question. I have just been informed that it is around 10 million. I presume that analysis comes from Gulf.

But, in any event, I understand that Gulf itself has approximately 200,000 shareholders, many of whom are public and private pension funds.

Now, these shareholders, if my understanding is correct, would realize about $13.2 billion from the proposed Socal-Gulf merger. Some $1.9 billion, almost $2 billion, is estimated to go to the Federal Government, give or take a little, I guess, from these shareholders in the form of capital gains taxes.

Now, that leaves $11.4 billion to be reinfused into the economy through that method. And do you think that these effects have been contemplated by your amendment?

Senator JOHNSTON. Oh, there is no question about it. You say it is going to be reinfused into the economy. The chances are it won't be reinfused into oil companies; it may be reinfused into the stock market, but that doesn't give you any additional capital.

What you are doing in effect is taking away from the new Socal-Gulf merged company $13.2 billion in assets or credits, or whatever you want to call it, saddling them with that debt which they are going to have to pay over a period of 10 years or whatever, in order to give people $11.2 billion, or whatever it is, which then they may put in the stock market, which creates no new assets, no new companies, it just runs up the cost of other stock—or they use it up to go to Las Vegas, or buy a boat, or whatever, all legitimate ends under our free enterprise system.

It doesn't penalize private pension funds except to the extent that they would make a quick profit now, which would not be realized later. I say that profit would be realized later, because the assets are there.

Senator HATCH. Let me ask you just one other question because the distinguished chairman would like to move on.

Do you know of any reason why the Mobil-Superior and Gulf-Socal mergers should not be judged according to the same standards as the Texaco-Getty merger? Is there anything about Gulf-Socal or Mobil-Superior that indicates to you that they deserve any special treatment or some heightened level of scrutiny?

Senator JOHNSTON. Each one of these mergers has its own peculiar advantages and disadvantages—and I have looked into the pros and cons of each one.

The reason I chose February 28—and legislation is a series of arbitrary choices, you can't cure the whole world, and so you have to decide which problems you are going to deal with and with what fairness—February 28 we thought was fair because that is the date upon which the legislation was initially discussed on the Senate floor and at which time we publicly stated that we are putting

companies on notice that from there on out we would attempt to have a moratorium.

Senator HATCH. Well, let me just say in closing that I know you believe that the free market is probably the best way of ensuring efficient utilization of capital, but the thing that worries me, Bennett, about your bill, is that it may directly interfere with the free flow of capital in our society, substituting Federal Government regulation and intervention for determining what may be the most efficient allocation of capital.

And even though it seems like whenever you have a big merger between two large companies, admittedly in an industry where there is plenty of competition even with the merger, that you are not really—that that is not as big a problem as it is, say, in the manufacturing industry where, for instance, the four top companies would control maybe 40 percent of that industry, where the four top big oil companies would control somewhere around 20 percent. It seems to me that it is very worrisome—it is very worrisome to me that we would do this in an artificial way with a moratorium at a time when these people have entered into these agreements, and not let the system of antitrust laws that should take care of anticompetitive and predatory and other type of antitrust conduct, should take care of them efficiently and well.

And that is what worries me about the approach you are taking. And that is why I think—I could spend a lot of time on other questions—there are so many questions that are unanswered by your legislation—it isn't simple, it's very, very serious at a very, very serious time in our country's history and serious vis-a-vis various companies who will be able to get away with it, while others will not in almost the same timeframe—that that's why I think it may pay to let the committee process run and operate and come to the right conclusion on this. And if you are right on this, then I will join you.

Senator JOHNSTON. Well, the difference is that if you waited that long, then these mergers which have not yet been consummated—Socal-Gulf, Mobil-Superior—would then be consummated.

Senator HATCH. That may be, but at least that may be better than what you are doing is what I am saying. What you are doing is artificially injecting an amendment into the process that may not work nearly as well, and may result in the demise of two companies that could ultimately survive as one company and do a great job for this country and for the consumers throughout the country.

Senator JOHNSTON. If I may say, I think the chances of these companies being better able to survive postmerger than they can right now is totally without foundation.

Senator HATCH. Well, we don't know.

Senator JOHNSTON. Well, we do know, for example, that Socal-Gulf would be burdened with $13.2 billion in debt which they do not now have, or at least half of that, representing the profit, is debt they would not now have.

It cannot be easier and more efficient for a new surviving entity, burdened with that kind of debt—it cannot be better able to survive than one with the same assets which does not have the debt.

Senator HATCH. Well, I think there are a lot of questions which go unanswered, and we could spend all day just on this question.

I apologize for taking as long as I have, but I have just begun to touch the surface of economic and other questions that just simply have to be asked. You just can't interject something like this and not expect it to have massive implications throughout our financial markets, and throughout our economic markets, and the consumer markets in this country.

Senator JOHNSTON. No doubt about that, but you get massive implications by doing nothing, too. That is probably the worst of the alternatives, it seems to me.

Senator HATCH. Well, except that you have laws in place that are supposed to take care of that, and I believe can take care of that and will take care of it if there is in fact anticompetitive conduct.

The CHAIRMAN. The distinguished Senator from New Hampshire, former Attorney General, able lawyer, glad to hear from you.

STATEMENT OF SENATOR WARREN B. RUDMAN

Senator RUDMAN. Thank you for that very warm introduction, Mr. Chairman, and I appreciate sitting here with my friend from Louisiana; we share something that is quite similar about oil—they produce it and we use it to keep from getting cold.

My interest in this whole area of antitrust goes back a long time, and I hope that in some of the things I am going to say I will address some of the questions, very able questions and searching questions, I might add, asked by the Senator from Utah, Mr. Hatch.

Mr. Chairman, let me just summarize briefly at the beginning here by saying——

The CHAIRMAN. You have a written statement. Would you want that put in the record?

Senator RUDMAN. I would like it to be put in the record, yes.

The CHAIRMAN. Without objection, that will go in the record and you can give us a résumé.

Senator RUDMAN. Mr. Chairman, the Senator from Ohio, Mr. Metzenbaum, in his very interesting and very colorful opening really was telling a very interesting story. We are not seeing corporate managers sitting with their consultants, accountants, and lawyers, developing business plans, business plans that will be best for their companies and their stockholders; we are not seeing slow, deliberate, thoughtful acquisitions. We are seeing a madhouse.

What we are seeing is a few people in this country, a very few people, who have a great deal of money and access to more, who are essentially starting to play Monopoly with real money. That is really what we are seeing.

Anyone who has gone into the history of what happened to the poor people at Gulf has to feel sorry for them.

Senator HATCH. But they have small market shares, Senator; I mean, how can you argue that?

Senator RUDMAN. I would like to address that now because I think the distinguished Senator from Utah's interpretation of the current antitrust laws is, to put it kindly, wrong. [Laughter.]

Senator HATCH. Well, I give great deference to the distinguished Senator from New Hampshire on antitrust, and I would be interested.

HERFINDAHL INDEX

Senator RUDMAN. I'm not here today to say that what is going on is necessarily bad—I don't know. I am here to say that current antitrust and tax policies are encouraging mergers among major corporations which may not be in the national interest.

For the Judiciary Committee's information, I did some calculations of the Herfindahl index, and I am going to tell you something very interesting. Your staff might want to do it itself. I think this is very illuminating.

Under the current merger guidelines, it would not automatically trigger a challenge—would not automatically trigger a challenge—if Exxon, Arco, Amoco, Chevron, Texaco, and Mobil were to merge to form one single company.

Here is the Herfindahl index—I've used it in the past, and I think I know how to add and subtract and get the square.

The fact is that its use is imperfect in this particular market. Under present law we could see a merger which would result in companies with revenues of over 300 billion, which is about half the revenues of the Federal Government. That single statistic, more than any other I have heard, represents sufficient justification for the Federal Government to place at least a hold on the merger activities of these corporations in order to qive us some time to reassess our policies. At that time, we might decide that that was all right—maybe it is. I don't know, I am not prepared to say today whether it is or it isn't.

The legislation we propose targets a specific industry—not the best kind of legislation—so I want to address myself to that particular point.

Petroleum is very vital to this country's well-being. We have to be certain that major changes in the industry which would threaten the competition we traditionally embrace will not adversely affect this country. For example, the competition sparked by middle tier and small companies helped to weaken OPEC's control of the world petroleum market. Reason suggests that some of the proposed mergers would reverse this beneficial trend.

First, three of the four companies which make up the ARAMCO partnership in Saudi Arabia have entered into merger agreements with companies outside of that partnership. Evidence indicates that the ARAMCO partnership is unable or unwilling to stand up to Saudi Arabia and other OPEC countries.

The proposed mergers would serve only to strengthen OPEC's position.

Second, a number of OPEC countries—for example, Saudi Arabia and Kuwait—have indicated that they would like to purchase refineries and gasoline stations in the United States.

The Federal Trade Commission has indicated that it would allow mergers in the oil industry if they would divest themselves of some of their refineries and gas stations. Since most of the oil companies in this country are trimming down to size and have no interest in

these facilities, it's unlikely that they would be willing to purchase any of these refineries or these gasoline stations. Consequently, among some oil industry experts with whom I have talked, the only buyers might well be OPEC countries and their representatives. The result would be an increase in control for OPEC, which should concern all of us.

Third and last, I doubt seriously whether many of the merging companies would be able to maintain current exploration levels while attempting to repay the enormous debt that would be incurred to finance the proposed mergers.

I will skip over this point because I think my friend from Louisiana has covered that in depth.

The method adopted by the oil companies to gain FTC approval of the proposed mergers also raises questions which need to be addressed. The FTC would challenge these mergers unless the companies were willing to divest certain property. I am not sure that is the proper solution in this case. It is the historical solution—divest certain property, get smaller, and have more competition—and obviously that seems to be all right. That is traditional thinking. Perhaps it is still right, but, I am not sure that it is. It is very difficult to determine the impact of such divestiture, because it is likely to have a heavy impact on independent refineries, independent gas stations, and employment in general.

Independent refineries and gasoline stations are dependent upon the major development companies for crude and for gasoline.

Some of the mergers being proposed result in companies with no surplus crude selling to independent refiners.

Finally, are these mergers really necessary? We hear arguments that the mergers are necessary for the oil companies to meet the rising cost of exploration. But if that is so, why is it that the Gulf Corp. would have far preferred to remain a single entity? Gulf did not agree to merge because it believed an increase in size would enable the newly merged company to better spread the risks of exploration. The merger was proposed to escape the bid of T. Boone Pickens to control the company.

I haven't met Mr. Pickens, but he seems to have a lot of people scared, apparently with good reason.

In fact, the large companies don't need to merge in order to meet rising exploration costs. All of these companies engage in joint ventures to spread costs in association with their exploration. In addition, Congress has provided tax incentives which oil companies claimed were necessary to meet that problem. Instead of exploration, we seem only to have fostered conglomerates and merger mania.

I do not have answers to the questions that I have raised, Mr. Chairman. It well may be that my fears are groundless. However, when dealing with an industry as vital to our national security and economic wellbeing as the petroleum industry, I think it is imperative to explore the issue in depth.

I can't believe that the industry is so threatened that it could not survive a short period of the status quo while we sort out the factors and interests which ought to be considered and balanced to arrive at a rational national policy. I don't want to be stampeded

in the decisionmaking process only to find 2 or 3 years from now that a hasty decision resulted in a regretted decision.

I hope, Mr. Chairman, that you and the members of the committee will agree that a cooling-off period is in order. You know, Ben Franklin said it very well when he talked about business in America. He said: "Drive thy business, let not it drive thee."

That is quite the reverse of what the Secretary of Defense in the Eisenhower administration once said about what is good for business in America. What is good for the oil companies may well be good for America. But, Mr. Chairman, let's find out.

[The following was received for the record:]

STATEMENT BY SENATOR WARREN B. RUDMAN

Before The

SENATE JUDICIARY COMMITTEE

March 15, 1984

Mr. Chairman, members of the Judiciary Committee, during the past few weeks much has been said about the recent wave of merger activity in the oil industry. What we hear most often is that Wall Street attorneys are dropping their briefcases, putting on hard hats, and drilling for oil in lower Manhattan. I am not here today to say that this is necessarily bad. Instead, I am here to say that I am concerned that current antitrust and tax policies are encouraging mergers among major corporations which may not be in the national interest. For example, the current merger guidelines would not automatically trigger a challenge even if the six largest oil companies, Exxon, Arco, Amoco, Chevron, Texaco, and Mobil, were to merge to form a single company. In other words, under present law we could see a merger which would result in one company with revenues of over $300 billion, almost half the revenues of the federal government. That single statistic, more than any other I have heard, represents sufficient justification for the federal government to place a hold on the merger activity of these corporations in order to give us time to reassess our policies.

The legislation we propose would target a specific industry, and to justify the action I must address my remarks to that industry. At present, although there is significant concentration in the petroleum industry, mid-size companies have ensured vigorous competition all the same. Because petroleum is so vital to this country's well being, we must be certain that major changes in the industry which would threaten the competition we have traditionally embraced will not adversely affect our nation. For example, the competition sparked by middle tier and smaller companies helped to weaken OPEC's control of the world petroleum market. Reason suggests that

some of the proposed mergers would reverse the beneficial trend. First, three of the four companies which make up the Aramco partnership in Saudi Arabia have entered into merger agreements with companies outside of that partnership. Evidence indicates that the Aramco partnership is unable or unwilling to stand up to Saudi Arabia and other OPEC countries. The proposed mergers would serve only to strengthen OPEC's position. Second, a number of OPEC countries, for example, Saudi Arabia and Kuwait, have indicated that they would like to purchase refineries and gas stations in the United States. The Federal Trade Commission has indicated that it would allow mergers in the oil industry if the merging companies are willing to divest some of their refineries and gas stations. Since most of the oil companies in the United States are trimming down in size, it is unlikely that they would be willing to purchase any of the refineries and gas stations which would be put up for sale. Consequently, the only buyers would be OPEC countries. Again, the result would be an increase in control for OPEC. Third, and last, I doubt seriously whether many of the merging companies would be able to maintain current exploration levels while attempting to repay the enormous debt that would be incurred to finance the proposed mergers. Once again, the result would be an enhanced OPEC position in the world market. This would not be in the best interest of this country.

The method adopted by the oil companies to gain F.T.C. approval of the proposed mergers also raises questions which need to be addressed. The F.T.C. would challenge these mergers unless the companies are willing to divest certain properties. I am not sure that this is the proper solution. It is difficult to determine the impact of such divestitures, but they are likely to impact heavily on independent refineries, independent gas stations, and employment in general. Independent refineries and gasoline stations are dependent upon the major development companies for crude oil and gasoline. Some of the mergers being proposed would result in companies with no surplus crude oil to sell to independent refineries. Also, what will

happen to independent gasoline stations as new, larger companies expand their own retail outlets? Without independent refineries and retail stations, we would be faced with a total vertical integration of the industry. Is this the result we want?

Finally, are these mergers really necessary? We hear arguments that the mergers are necessary for the oil companies to meet the rising costs of exploration. But, if that is so, why is it that Gulf Corporation would prefer to remain a single entity? Gulf Corporation did not agree to merge because it believed that the increase in size would enable the newly merged company to better spread the risks of exploration. The merger has been proposed only to escape the bid of T. Boone Pickens to control the company. In fact, the large companies do not need to merge in order to meet rising exploration costs. All of these companies engage in joint ventures to spread costs and risks associated with exploration. In addition, Congress has provided tax incentives which oil companies claimed were necessary to meet that problem. Instead of exploration, we seem only to have fostered conglomerates and merger mania. Is it not time to reassess the whole range of incentives before we are faced with a completely restructured industry?

I do not have answers to the questions that I have raised. It may be that my fears are groundless. However, when dealing with an industry as vital to our security and economic well-being as is the petroleum industry, I think it is imperative that they be explored in depth. I cannot believe that the industry is so threatened that it could not survive a period of continued status quo while we sort out the factors and interests which must be balanced to arrive at a rational national policy. I do not want to be stampeded in the decision making process only to find two or three years from now that a hasty decision resulted in a regretted decision. I hope, Mr. Chairman, that you and the members of the Committee will agree that a cooling-off period is in order. In another context, Ben Franklin said "drive thy business, let not [it] drive thee." I think we would do well to heed his advice.

The CHAIRMAN. Thank you very much, Senator.

The distinguished Senator from Ohio.

Senator METZENBAUM. We have a number of important witnesses here, Mr. Chairman, and I am anxious to let them have an opportunity to be heard. I think their testimony will go to the issue at hand. I am going to withhold my questions.

I agree with Senator Rudman.

Senator RUDMAN. Thank you very much, Senator Metzenbaum; I am really not too surprised.

Senator HATCH. I am glad Senator Metzenbaum let us know where he stands on this issue. [Laughter.]

The CHAIRMAN. You have already made up your mind?

Senator METZENBAUM. I did.

Senator HATCH. That's amazing to me with all these unanswered questions.

Senator Rudman, I haven't seen where you and I disagree much on antitrust law. From your statement, you seem to say that you don't like the present merger guidelines—and I am not sure I like them either. I am not sure what is right and what is wrong here. All I know is there are a lot of unanswered questions.

You seem to be saying that you are not sure whether this is good or whether this is bad, but you think there needs to be a moratorium so it can be looked at. Well, that may be.

But I think those questions that I have asked as to what happens to these shareholders, these pension trusts, and all these other little people all over this country that are going to be hurt—what is going to happen to them? What is going to happen to the two companies—not just the two companies; I look at the Mobil-Superior merger and I don't see any anticompetitive effects there; I don't see anything forbidding that in antitrust law.

Now, maybe just one question, and that is this—and I will limit it to this: Do you see something wrong with Hart-Scott-Rodino, or any of the other antitrust laws, that could not take care of this problem, or do you just think it is such an exigent, urgent problem that we need exigent, urgent approaches, even though you are not sure which is right?

Senator RUDMAN. Senator Hatch, let me answer it this way. I think that we have a very difficult job of balancing some interests here.

Senator HATCH. That's not antitrust; that may be public policy.

Senator RUDMAN. Well, I want to get to the antitrust in just a moment, but I think your question has within it certain aspects of what equity is, and I want to respond to that.

It seems to me that to balance the interests of these stockholders, these institutional investors, over the next 6-month period against what could be—could be, I will not say would be—a degree of concentration of the industry that could be disastrous to the best interests of the country, is a balance on which I would have to come out on the side of what was best for the country as a whole. I do recognize that there are people out there who may not make as much money as they thought they would. I imagine anybody who is watching this on television, who bought Gulf at 29 and is going to sell it to Socal for 80, must be taking bicarbonate of soda by the

teaspoonful. I can understand that. But, you know, I think we have some bigger interests.

Now, coming to your specific question, it seems to me that the antitrust laws, as they go back in history—and, of course, you and I have discussed their genesis with conservative Republicans—they come out of the Theodore Roosevelt administration—those laws——

Senator HATCH. Don't forget the liberal courts that have expanded them quite noticeably.

Senator RUDMAN. That's true. And as they have been modified, it seems to me may not look at what are now world markets in many ways. To give you the flip side of the issue, I am not sure the antitrust laws in the case of the steel industry really apply anymore when you look at worldwide competition.

Senator HATCH. Right.

Senator RUDMAN. And by the same token, as you look at the antitrust laws in the oil companies, we have to start looking at some other factors that do not apply. I mean, for instance, I am sure my friend would agree with me that if you could take Exxon, Arco, Amoco, Chevron, Texaco, and Mobil and put them together and not violate Herfindahl, something is wrong someplace.

Senator HATCH. I am not sure you can do that.

Senator RUDMAN. Oh, I think I am correct.

Senator HATCH. I don't think I agree with that.

Senator RUDMAN. Oh, I don't think the Justice Department or the FTC would lie still, but I am saying that the guidelines would not be violated.

So my answer is yes, they may have to be changed.

All I am saying is let's have a thorough airing of this issue; let's look at the tax implications, the antitrust implications—and I am prepared to let the status quo stay at the end of the 6 months. I am not antioil at all. We need oil in this country, and if this is the way to get more at a cheaper price, I am all for it.

But I am just not sure.

Senator HATCH. Well, you and I seem to be arguing for the same thing. I would like to see the committee process, not because it will delay, but because these committees are expert at looking at these things, and perhaps we can come to a more astute and more intelligent approach to it.

You admit here today that there are a lot of questions just can't simply be answered. I have to admit that. I have asked them. And I have only asked a small smattering of questions that need to be asked in this matter as far as the effects it will have on society in general, people in particular, the two companies, other companies, et cetera.

But, you know, I can't say that I have disagreed with much of what you have said. All I can say is that if you have this moratorium put into place, is this not an artificial injection of the Government into a situation that it might not really have a place to be injected, and it might cause a lot of problems that literally will hurt an awful lot of people in this country?

These aren't just two big companies; these are made up of hundreds of thousands—maybe not hundreds of thousands, but thousands and thousands of shareholders and other entities, and they are the people who are going to get hurt.

Mr. Lee is probably going to survive no matter what happens; Mr. Keller will survive; but what about all those people, including society in general, because we all of a sudden decide to inject the Federal Government into something when we have adequate laws to take care of it?

If the guidelines aren't right, let's change the guidelines.

Senator RUDMAN. Well, let me just answer that in two ways—and I will be very brief, as I know the chairman is anxious to move on. I appreciate his indulgence

Just let me say, first, in terms of your first point, if we go through the normal process here and decide a year or 18 months from now—and, you know, we won't be in session much this year—that really we ought to have some changes, I get the faint feeling there are people circling around now watching what's happening, ready to move, and we just may have a lot of companies grabbed up in one fell swoop. There are people out there who are really playing a high-stakes game.

No. 2—and I don't mean to be flip, but it's the best way that I can explain it. As far as all those people who bought at 29 and want to sell at 80, who may have to wait 6 months to sell at 65—I am reminded of what my grandfather once told me about the stock market. He said "Bulls make money, and bears make money, and hogs get slaughtered."

And that's about the way I feel about it.

The CHAIRMAN. Thank you very much, Senator.

Senator RUDMAN. Thank you, Mr. Chairman. I have to go to another meeting, I'm a bit late for it.

The CHAIRMAN. The distinguished Senator from Oklahoma, Mr. Nickles, we are glad to have you with us.

STATEMENT OF SENATOR DON NICKLES

Senator NICKLES. Thank you, Mr. Chairman. Mr. Chairman, I will just make a few brief remarks. I appreciate your hospitality. My original intention was just to come and be a spectator primarily and maybe make a few comments about the legislation.

One of the reasons I am here—and I am not a member of the Judiciary Committee, we have hearings scheduled on this legislation before the Energy Committee of which I am a member—is because I am aware of the merger mania which is taking place both on the stock market and perhaps even more so in Congress. I wanted to participate in this hearing before this action ends up on the floor again. And it is quite likely that it will be on the floor before we have the hearings in the Energy Committee.

I do not really like some of the mergers that have taken place. I have some reservations about them and I would have much preferred that some of those companies which have been merged would have remained independent. Some of those companies have been in my State and it would certainly be my preference—as it would be for all of us when we have fairly large companies in our State—to see those companies maintain their independence.

With that in mind, I have looked at this legislation and some of the other proposals that have been pending or floating around, and I have some serious reservations concerning those proposals.

Many of them are good politics, maybe they capitalize on the merger mania that's out, maybe they capitalize on the antibig oil—that's two words, a lot of times you hear it used as one—but, quite frankly, I think that the proposals, although they may be good politics, are poor economics and certainly antifree enterprise.

To highlight some of the reservations that I have on the bill that is before this committee, and the Johnston proposal in particular, I will discuss my major concerns.

RETROACTIVE EFFECT

One, and maybe first and foremost, is that it is retroactive, which in my opinion would be unconstitutional. That is more for this committee to decide than the Senator from Oklahoma, but I would certainly have some reservations about it's constitutionality in light of the fact that it is retroactive.

I have problems with a Senator saying, "Yes, we introduced legislation on this date and we are going to assume that it is effective from the date of introduction." This Senator doesn't like the windfall profits tax, and if I introduce repeal legislation tomorrow can I say that effective March 16 the windfall profits tax will be eliminated from that day forward?

Anyone can introduce legislation, but I really don't think it should be effective until after it has passed both Houses. This legislation would certainly affect two of the major mergers, the Socal-Gulf merger and the Mobil-Superior merger, which have been discussed, because they were "on notice" when the bill was introduced.

EFFECT ON STOCKHOLDERS

Second, my biggest objection is I have a hard time telling a stockholder that he cannot sell his stock to someone. To me that is a fundamental right. A person buys stock with the expectation that he can sell it. If we in Congress superimpose our authority and say no you can't sell it, I think we are certainly infringing upon that individual's economic right.

In two of the mergers that have been discussed—the Texaco-Getty merger and the Mobil-Superior merger—you had large stockholders who desired to sell their stock. If we allow this legislation to go through, even though Texaco-Getty has been tentatively approved but the theory is the same, we would be telling those stockholders they do not have the right to sell their stock.

And to me I think that would really be a fundamental miscarriage of justice.

I did not like seeing Getty sold. The company has a lot of physical presence in Oklahoma, and I would much prefer Getty remaining independent, but they also had a majority stockholder who wanted to sell his stock. And I think he should have the right to sell that stock, and I do not like to think that Congress would say no. And the same thing with the Keck family in regards to Superior Oil—they should have that right. Stock is on the market, it is on the market to be bought and sold.

Another part of this legislation limits royalty trusts from stock purchases and, again, I think that is an infringement on individual rights and liberties which we should not involve the Congress.

EFFECT ON THE OIL INDUSTRY

A lot of people wonder what is the effect of these mergers and what will it do to the oil industry? I am very concerned about what it will do to the oil industry. I think if we put a cloud over oil companies by saying the top 50 oil companies cannot be merged, really a black cloud; you will see a depressing effect on their stocks—I think we have seen that in a few stocks already. And certainly that will hurt investment in the oil and gas industry, and likewise that will hurt future production.

We have heard a lot of people say they want future exploration and production. Just the very threat of a moratorium and the threat of this type of legislation can be most detrimental to energy security, energy investment, and energy production.

EFFECT ON THE CREDIT MARKET

A lot of people have said and made comments that this will take 29—I think we even heard the figure $100 billion—away from the credit market. I have heard people claim that this is financed by the taxpayers.

I did not know that the Federal Government owned all the available credit that is out in America today. They do not own it; people own it. And if people are willing to loan that money, they should have the right. And if we are going to pass legislation, as alluded to by several people, that says if individuals borrow money and use that money to buy oil companies, that they then cannot deduct the interest on that money, well let's make that across the board, let's don't single it out for hostile, or nonhostile, or oil companies alone; let's don't single out energy companies. That is bad legislation. And I think most people would realize that.

To say that this borrowed money is lost, or is buried, or is not put back into the economy I think is not looking at economic reality. Economic reality is the fact that, yes, somebody is going to be buying that stock, they are going to take that money and purchase someones stock with it. Those sellers will, in almost all likelihood, be putting that money right back into the stock market—maybe they will put it in the energy industry, maybe they won't. That is that individual's right. We in the Government shouldn't prohibit that right.

EFFECT ON EXPLORATION AND PRODUCTION

Now others have said this could have a negative impact on production and exploration. Well, some mergers have positive impacts. I will give you one example, Mr. Chairman, and I won't take but just a second. In 1976, Southland Royalty Co. took over Aztec Oil & Gas Co. whose stock before the merger was going at $14 a share but was worth roughly $36 a share. Southland bought the stock at $32 a share, for $160 million. They did expand production of that new acquisition by drilling several hundred new wells on old Aztec property. They did increase the value because they were a more ag-

gressive management, they utilized the properties that that company had. And it really turned out to be a good deal for all participants—for the acquiring company, for the company that was sold, and for Uncle Sam. There was more activity, more investment, more profits, more taxes returned—so that was a positive thing.

EFFECT OF QUICK-FIX LEGISLATION

I debated 2 weeks ago against this legislation and at that time it said that there couldn't be a merger if a company had over 10 million barrels of reserves. This legislation is changing all the time. Today it says 100 million barrels of reserves. I have asked for a list of affected companies and the list that I have received goes back to 1982. Well, assets and reserves have changed substantially, so I am not sure that anyone knows exactly the number of companies that are involved and which companies are involved.

So I think we have got some grey areas there.

Senator HATCH. Senator, I think what you seem to be saying is that this amendment has undergone a number of significant changes since it was first offered on the Export Administration bill.

Originally, as I recall, it would have penalized companies—and I hope somebody will correct me if I am wrong—but it would have penalized companies that wanted to merge by prohibiting them from ever—forever—from getting any Federal lease or right of way.

Senator NICKLES. The Senator is correct.

Senator HATCH. Now, I understand that the present language, as now drafted, may not prevent a proxy-fight liquidation type scenario. Do you know if that is true?

Senator NICKLES. I think the Senator is correct. Let me make just a couple of concluding comments.

Yes, the original legislation introduced by Senator Johnston said that, yes, if there was a merger during that 6-month period, the companies involved would be forever prohibited from any new Federal oil and gas leases, which would have a disastrous effect on any of those companies. Under those circumstances there is just no way in the world there would be a merger in those companies. He's changed the legislation; I think it is better now—it is just a flat moratorium. But I still think it leaves a lot to be desired.

For example, you could have some situations wherein you may well have some companies that need to merge. Not all oil and gas companies are very healthy; some are having difficulty. Maybe that merger would help them to be able to survive; maybe it would help them be able to compete. There are all kinds of different factors.

If we place a blanket moratorium the effect would be most detrimental. Such a moratorium would prohibit an outside company, United States Steel for example, from acquiring one of these companies. And maybe an outside merger could be helpful to those companies.

A blanket moratorium I think leaves a lot to be desired. It's for 6 months, and some say, well, what's wrong with 6 months? Well, what will 6 months solve? And that is the big question I wanted to ask. What happens during that 6 months? Six months could very well become 1 or 2 years.

I think Senator Specter made a good suggestion when he expressed some reservations about the moratorium: if one has specific recommendations of what could or should be done, then Congress, this committee, or the appropriate committees might consider those actions, and everyone could have imput and know what would happen. But to have a blanket moratorium to just see what comes up, and then during this 6-month period of time ask the Attorney General, who probably knows little if anything on energy—the same thing with the Secretary of the Treasury, the Secretary of Interior——

Senator METZENBAUM. That has been changed, Senator.

Senator NICKLES. I hope it's been changed. It shows again that this legislation is not well thought out and needs to be changed.

Senator METZENBAUM. That has been changed to a panel of nine people, four appointed by the leadership of the House, four by the Senate, and one by the President.

And I think it's fair to say, Senator, that if you are indicating that there are some portions of the bill that you have difficulty with but that you support the overall objective and thrust, then I think you would find that the cosponsors would be receptive to sitting down and working with you on the language.

Senator NICKLES. I will be happy to discuss this with the Senator from Ohio, who I have a great deal of respect for even though I usually don't agree with him on these particular measures. But I will be happy to discuss this with him, because I do have some problems. And I am glad to hear that you have decided to scrap this report from every Secretary in the Cabinet.

I think it is becoming clear that there are some problems with this legislation. My guess is that this commission is if we have a fair approach on the commission, their conclusion will be that nothing needs to be done. Basically my guess is that they will say that it is a competitive industry and that the mergers are not noncompetitive. My guess is that they will also say that the money doesn't disappear in a merger, but that the money does work its way through the financial system. And my guess is also that they will say that mergers should be looked at individually.

But I appreciate the Senator indicating a willingness to work on the legislation. I am open to the need to legislate, but as I said, I have some reservations about Congressional moratoriums. This is so even though I don't particularly care for all the mergers that have taken place or possibly may take place.

But I also have a very severe abhorrence to the Federal Government saying no you can't sell your stock to somebody. If an individual acquired that stock with the expectation he could sell it to anybody who wanted to buy it, as long as he is in compliance with antitrust laws, I think we would be doing a violation to that individual, to his rights, and, as Senator Hatch mentioned, to the millions of people that are dependent on that stock through pensions and other investments.

Thank you, Mr. Chairman and members of the committee.

If the Chairman would indulge me, I would like to participate in the panel and hear some of the witnesses, their testimony.

The CHAIRMAN. We will be glad to have you come up here and join us, Senator.

Senator NICKLES. Thank you, Mr. Chairman.

The CHAIRMAN. Any questions for Senator Nickles? If not, we will pass on.

Senator METZENBAUM. I want to ask Senator Nickles just one question.

The CHAIRMAN. Excuse me, I didn't think you had any questions.

Senator METZENBAUM. Just one. Senator, would it bother you if, as indicated in the media, in the Washington Post today, if Saudi Arabia and Kuwait, as a result of the Socal and Gulf merger, were to wind up owning 15,000 gas stations in the United States?

Would that bother you?

Senator NICKLES. I would think it would be something we would want to examine.

Senator METZENBAUM. It would bother you?

Senator NICKLES. I've told the Senator I am bothered by some of the mergers. I am also bothered by the cure that is proposed before us today, too

Senator METZENBAUM. I thank you, Mr. Chairman.

The CHAIRMAN. Come on and join us, Senator, if you would like to.

Senator JOHNSTON. Mr. Chairman, may I simply state that copies of our legislation will be available at 9 o'clock in the morning either in 136 Hart Building or SD-312—that is my office—and the Energy Committee and we will have final copies.

The CHAIRMAN. All right. No charge for that publicity. [Laughter.]

Senator HATCH. Bennett, could I ask you, will this bill draft be different from what you circulated in your "Dear Colleague" yesterday? Will they be the same or are they going to be changed?

Senator JOHNSTON. Slightly different.

Senator NICKLES. Besides the composition of the commission are there any other major differences?

Senator JOHNSTON. No major difference, no.

Senator NICKLES. You would still leave the 100 million barrels?

Senator JOHNSTON. Still the 100 million, which is the 50 major companies; still the same basic mechanism with respect to royalty——

Senator NICKLES. Would the Senator give us a list of those companies? Do you have something more recent than the 1982 list?

Senator JOHNSTON. Yes; we have some lists right here.

The CHAIRMAN. If you all could get together—I tell you, we've got a lot of important witnesses here, and I'm afraid they are not all going to be heard.

I think we are going to have to limit these witnesses to 5 minutes, and we will put your entire statements in the record. We will limit you to a 5-minute résumé, and then questions, because the Senators have a good many questions.

Our next witness is the Honorable Michael Pertschuk, Commissioner of the Federal Trade Commission. Mr. Pertschuk, we are glad to have you with us.

And I believe you have Mr. Muris with you, don't you?

STATEMENT OF HON. MICHAEL PERTSCHUK, COMMISSIONER, FEDERAL TRADE COMMISSION, ACCOMPANIED BY EDDIE CORREIA, ATTORNEY-ADVISER

Mr. PERTSCHUK. I have with me Mr. Eddie Correia, who is an attorney-adviser to me.

The CHAIRMAN. All right, we are glad to have him. You may proceed.

Mr. PERTSCHUK. Thank you very much, Mr. Chairman. I certainly will try and shorten my statement.

The rush of oil companies to merge is radically restructuring the oil industry.

The CHAIRMAN. I've got a light here; as long as it's green, you can talk; when it turns red, you will stop.

Mr. PERTSCHUK. Yes, sir. Never before have such massive companies amassed such formidable lines of credit to acquire competitors of such size and strength. And this consolidation is taking place in that industry which contains the very largest corporations in this country; 6 of the top 10 industrial corporations in the United States are oil companies.

It may be that Senator Hatch is correct, that the antitrust laws, if applied rigorously, could have prevented much of the current merger wave. But it seems to me that there is little doubt that the current merger wave has been triggered in large part by the administration's lax antitrust enforcement policies.

Business Week reported on February 6 that "the Reagan administration's hands-off policy has been, in effect, enabling legislation for the current merger wave;" 9 of the 10 largest mergers in history, whether or not Socal-Gulf is included, have occurred during this administration; 8 of the 10 mergers on this list involve oil and gas companies. The only merger on the top 10 list occurring during a prior administration was only one-third as large as the $10 billion Texaco-Getty acquisition.

And the epidemic of large oil mergers is hardly spent, as other witnesses have indicated.

There are two sources of concern over these mergers, Mr. Chairman. There are antitrust concerns, and they are serious, over threats to competition in particular markets; there are also separate and equally serious industrial policy issues which fall outside the traditional focus of antitrust, including those issues of diversion of capital from more productive uses.

Let me turn first to the antitrust issues.

It is clear that most of these oil mergers have been driven by the desire for crude oil, which is much cheaper to acquire on Wall Street than through exploration and drilling.

One of the stock arguments defending oil mergers is that the industry, particularly at the level of crude reserves and production, is not highly concentrated. And we agree that a conventional analysis of horizontal concentration shows an industry which is much less concentrated than steel or autos, for example.

Senator HATCH. Would another word for that be "highly competitive"?

Mr. PERTSCHUK. No; it is not highly competitive. And I think the thrust of my testimony, which I stated fully in my written state-

ment is that there are other factors in this industry which mean that the raw figures, based on a supposition of a world market showing low concentration figures, are complicated by other anti-competitive factors.

Senator HATCH. I will read your complete statement.

Mr. PERTSCHUK. Thank you very much, Senator Hatch. I am rushing, Mr. Chairman, to get through.

One of the most serious concerns is not the threat of horizontal collusion, but the threat of the cutting off the sources of supply for independent refiners and marketers, threatening vigorous competition downstream.

And this is a very serious area of concern.

The degree of vertical integration in this industry, the ability of a few companies to influence supply and demand at one level of the system, by controlling another level, the prevalence of exchange agreements, the frequency of joint ventures, the degree of information exchange, the pervasiveness of joint pipeline ownership, the tax incentives which encourage major companies to divert crude through their own vertically integrated operations, the incentives of the major companies to eliminate the independent sector of the industry, and the not infrequent historic examples of price fixing in the past, all suggest this industry is far from the textbook model.

A simple assessment of horizontal market shares may miss the vast forest of potentially anticompetitive phenomena.

There are also serious problems associated with large oil combinations which fall outside of traditional antitrust analysis.

In particular, the diversion of capital investment for more productive uses, the potential and real waste of financial and human resources in takeover fights, the tying up of massive amounts of capital for acquisition, do not fall into traditional antitrust analysis as applied by the Commission and the courts—but they are serious problems. And if they are to be taken into account, Congress must take action.

Do companies divert capital from exploration and other productive investment when they use billions of dollars in cash and credit to buy up other firms?

The answer is most certainly yes. In lining up a credit line to buy Gulf, Mesa publicly noted that its capital spending plans for 1984 had to be cut in half. Oil companies openly admit that they need new reserves, and among the two choices, drilling or buying another company, merging is cheaper.

Our staff at the FTC found the exclusive motive for the Texaco-Getty acquisition was to gain control of Getty's crude oil.

Mr. Chairman, your light is up. I support the basic thrust of the legislation proposed by Senators Johnston, Metzenbaum, and Rudman.

Thank you very much.

[The following was received for the record:]

TESTIMONY OF MICHAEL PERTSCHUK
COMMISSIONER, FEDERAL TRADE COMMISSION
BEFORE THE SENATE JUDICIARY COMMITTEE

March 15, 1984

The rush of oil companies to merge is radically restructuring the industry. Never before have such massive companies amassed such formidable lines of credit to acquire competitors of such strength and size. This consolidation is taking place in that industry which contains the very largest corporations in the country. Six of the top ten industrial corporations in the U.S. are oil companies.

There is little doubt that the current merger wave has been triggered in large part by the administration's lax antitrust policies. Business Week reported on February 6 that "the Reagan Administration's hands-off policy has been, in effect, enabling legislation for the current merger wave." Nine of the ten largest mergers in history (whether or not Socal-Gulf is included) have occurred during this administration, as shown in the table below.

TEN LARGEST CORPORATE MERGERS

COMPANY/ACQUIRER (OTHER SUITORS)	COST (IN BILLIONS)	TERMS	DATE ANNOUNCED
Gulf/Socal* (Arco, Kohlberg Kravis, Mesa Petroleum)	$13.4	100% cash	3/5/84
Getty/Texaco (Pennzoil)	$10.1	100% cash	1/6/84
Conoco/Dupont (Seagrams, Mobil)	$7.4	40% cash 60% stock	7/6/81
Marathon Oil/ U.S. Steel (Mobil, Allied)	$6.5	51% cash 49% notes	11/19/81
Southern Pacific/ Santa Fe	$5.2	100% stock	9/27/83
Connecticut General/INA	$4.3	100% stock	11/9/81
Texasgulf/Elf Aquitaine	$4.2	100% cash	6/26/81
Cities Service/ Occidental (Gulf Oil, Mesa Petroleum)	$4.0	46% cash 55% notes	8/13/82
Belridge Oil/ Shell Oil	$3.6	100% cash	9/30/79
St. Joe Minerals/Fluor (Seagrams)	$2.6	45% cash 55% stock	3/31/81

*Pending.

Eight of the ten mergers on this list involve oil and gas companies. The only merger on the Top Ten list occurring during a prior administration was a third as large as the $10 billion Texaco-Getty acquisition. And the epidemic of large oil mergers is hardly spent. The March 7, 1984 Wall Street Journal reports industry analysts are targeting a list of second tier takeover candidates, including Pennzoil, Phillips 66, Superior, Kerr-

McGee, Hess and Sun. As you know, since that report, Mobil has agreed to buy Superior for $5.7 billion.

In the face of this radical restructuring of the oil industry, virtually no policy proposals or even questions emerge from the Reagan administration. The most that we see from the antitrust agencies, the Commerce Department and the Department of Energy is passive spectatorship, coupled by occasional attempts to justify after-the-fact the latest acquisition. Energy Secretary Hodel said recently: "An argument could be made by Texaco that, in order to compete effectively with Exxon, they need to acquire a smaller company like Getty." With all due respect to Secretary Hodel, justifying a merger by a company with $47 billion in sales to compete with a company with $95 billion in sales gives new meaning to economies of scale. If taken seriously, it would justify two-company industries throughout the economy.

But we need more than wishful speculation that everything must be alright because the free market produced it. Yet the administration opposes oil merger legislation, its antitrust standards are the flimsiest in history, it suggests no serious study of the ramifications for reducing exploration, it gives no hint that it is cognizant of the distortive impact of the tax code on stimulating mergers, it expresses no concern about tying up capital when the capital markets are squeezed dry by federal borrowing. In short, no one in the executive branch is minding the store, and any steps to address this onrush of acquisitions will have to be taken by Congress. I continue to believe that

Congress should enact specific limitations on oil company mergers while we gain answers to a number of crucial questions about the long-term effects of these mergers, particularly while this administration is blissfully unconcerned.

Antitrust Concerns

There are two sources of concern over these mergers -- antitrust concerns over threats to competition in particular markets and industrial policy issues which fall outside the traditional focus of antitrust, including diversion of capital from more productive uses. Let me turn first to the antitrust issues.

Each oil merger presents different factual circumstances and therefore must be examined individually by the antitrust agencies. My objections to the Commission's consent agreement permitting the Texaco-Getty merger, for example, focused on the absence of a long-term safeguard against Texaco cutting off supplies of crude oil to independent refiners which have depended on Getty. My tentative position is that the Commission should have gone to court to stop the acquisition instead of accepting the settlement. In the event we do initiate enforcement action my final views on liability will be based on the adjudicatory record. As to the Socal-Gulf merger, we have not yet been presented any recommendation by staff, and I have no views to present on the specific antitrust issues raised by that acquisition.

It is possible, however, to make some observations about generic antitrust problems that tend to flow from large oil company mergers and to gain some insights about why the current administration's policies have not deterred them.

First, most recent oil mergers are driven by the desire for crude oil, which is much cheaper to acquire on Wall Street than through exploration and drilling. This powerful incentive was apparent when Mobil tried to buy Marathon's rich Yates field by acquiring control of Marathon. A 1982 FTC Staff Report concluded: "... there was no indication that Mobil would have been able to produce oil from the Yates field more cheaply, or that Mobil could reduce its other costs of operation significantly through ownership of this source of crude oil." 1/ Our staff, in analyzing the Texaco-Getty merger, again concluded that the only reason Texaco wanted to buy Getty was to gain control of its crude and related mineral resources. (The value of the downstream assets which will be divested pursuant to the FTC's consent agreement constitute only 2% of the overall value of the acquisition.) That the desire for crude is driving these acquisitions -- rather than economies of scale or efficiencies from combining productive assets or the desire to profit from superior management techniques -- can be confirmed by almost any industry analyst. For example, Ernst von Metzch, an oil analyst with the Wellington Management Company, told the New

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1/ Mergers in the Petroleum Industry, Federal Trade Commission (September 1982) (cited below as the FTC Staff Report).

York Times: "The fact that you can buy these reserves for only four or five dollars a barrel at the stock market is important. You don't have to take the risks of drilling, which often involves exploration costs of more than $10 a barrel. Newsweek recently published a table based on data from Morgan Stanley & Co. and stock market values. It shows dramatically the difference between exploration prices per barrel and the price per barrel in acquiring stock.

It is true that there is some evidence that there is excess capacity in some companies in downstream assets, such as refineries and gas stations. John C. Sawhill, former Deputy Secretary of Energy, has suggested that mergers would help the oil companies rationalize their downstream facilities. This is a serious question and deserves study, but I am skeptical. The relationship between closing down or consolidating gas stations or even refineries and gaining total control of another company and its rich crude reserves seems tenuous. Why is such a radical consolidation needed to accomplish that objective?

One of the central arguments defending oil mergers is that the industry, particularly at the level of crude reserves and production, is not highly concentrated. I agree that a conventional analysis of horizontal concentration shows an industry which is much less concentrated than steel or autos, for example. The attached table, taken from the FTC Staff Report, shows the largest company, Exxon, had in 1980 only 9% of the free world's crude oil production. However, the antitrust concerns over crude acquisitions in cases that have arisen so far have not focused on the horizontal concentration of crude reserve assets, but on a "vertical" problem -- the threat to depriving the independent sector of the industry of loss of crude and refined product supplies. The FTC staff -- and on occasion the FTC Commissioners themselves -- have acknowledged there are such vertical problems, but the Reagan Commission has largely ignored them. The result has been a perfect blending of oil company desires and administration antitrust policy. The administration

Table VI B-1

World Crude Oil Production[1]
by Leading Domestic Companies
1980

Company	Production (000 barrels per day)	World Market Share (percent)	Free World Market Share (percent)
Exxon	4008	6.7%	8.9%
Texaco	3179	5.3	7.0
Socal	3009	5.1	6.7
Mobil	1991	3.3	4.4
Gulf	1169	2.0	2.6
Amoco	836	1.4	1.8
Sohio	716	1.2	1.6
Occidential	706	1.2	1.6
Arco	590	1.0	1.3
Shell	532	0.9	1.2
Conoco	459	0.8	1.0
Phillips	452	0.8	1.0
World Total	59,445	100.0	-
Free World Total	45,206	76.0	100.0
Top 4	12,187	20.5	27.0
Top 8	15,814	26.3	34.5

Source: Oil Daily, Apr. 5, 1982, at 12; Cent. Intelligence Agency, Economic & Energy Indicators 8 (Mar. 19, 1982).

1 Includes amounts purchased under long-term or special arrangements. In some countries, (e.g. Saudi Arabia), ownership of reserves by individual companies is not available. Instead, companies have long-term contracts providing access to production. In addition, the companies sometimes act as producers in such countries.

has focused on requiring limited divestitures in the "downstream" markets for wholesale distribution, pipelines and refineries, leaving the oil companies free to pursue their goal: acquisition of crude oil reserves. This accounts for the anomaly of the administration claiming tough antitrust action, while the pace of oil mergers accelerates.

This pattern is illustrated by the Commission's experience in the Mobil-Marathon attempted merger in December 1981. The Commission split 2-2 on whether to challenge Mobil's gaining control of Marathon's crude oil and refining assets. Chairman Miller's position, and the one the Commission argued in court, was to state expressly that the acquisition would not be objectionable if Mobil arranged a divestiture of Marathon's transportation, storage, and marketing assets. Commissioner Bailey and I dissented on the grounds that Chairman Miller's position ignored the "vertical" problem that Mobil would not follow Marathon's traditional pattern of supplying independents, particularly gasoline marketers. While the Commission was formulating this plan to save the acquisition, Mobil raced to find a buyer for the downstream assets. Unfortunately for Mobil, but fortunately for the rest of us, a private suit resulted in enjoining the acquisition, and the Commission ended up a bystander.

Similarly, in Texaco-Getty, the staff argued that there is a substantial risk that Texaco will cut off independent refiners, for example, Tosco, the largest independent refiner in California. This time the Commission has tossed a bone toward

the vertical problem by conceding that we should address a possible cutoff in the consent agreement, but it has done so with a half-hearted temporary supply requirement -- a remedy that has heretofore been rejected as an adequate solution for such a structural problem.

How important is the independent sector of the oil industry. The 1982 FTC staff report noted that the independents' share of gasoline sales in the country increased from 23% to 35% by 1980. 2/ In some local markets, of course, the share of independents is substantially higher. And, even if the share is in the 20-30% range, off-brand stations can impose a healthy price disciplining impact on the major integrated company's pricing policies. As the FTC staff report stated: "Independents have traditionally tended to induce price competition in markets." 3/

By emphasizing the threat of cutting off the independents, I do not mean to suggest that horizontal concentration of crude reserves is not entirely free from risk from an antitrust standpoint. It is unlikely that there is a textbook fluid world market for crude oil, in which crude flows freely to re-establish demand and supply equilibria over the entire planet. The world is, for better or worse, much more complicated than that. As we are painfully aware, OPEC -- when conditions give it market power -- restrains supply. We are still subject to random oil "shocks"

2/ FTC Staff Report, p. 290.

3/ Id., p. 287.

from reductions in supply from abroad. The fact that lightning has not struck lately does not mean that lightning cannot stike again. There are also periodic calls for import taxes on imported oil for other national policy reasons. As the FTC staff report stated: "Both history and well established national security interests strongly suggest that, as a practical matter, crude oil purchasers may not in the long term have the alternative of purchasing unlimited amounts of foreign crude oil. Accordingly, mergers which appreciably increase concentration in domestic crude oil markets may be of concern." 4/ These considerations all mean that we should be concerned about domestic as well as world concentration although crude oil concentration at the national level is still moderate, as noted in the attached Table taken from the FTC staff report.

The evidence also suggests that there is not a single market for crude oil, even within the United States. As the 1982 FTC Staff Report notes, there may be particular geographic and product markets for crude oil within the U.S. 5/ For example, previous FTC staff investigations strongly suggested that low quality crude oil in the west coast area was a separate market with particular supply and demand considerations. In the Texaco-Getty matter, the Commission's proposed complaint alleges a market in the sale of heavy crude oil in the State of California. Further, as the staff argues in Texaco-Getty, the

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4/ Id., p. 149.

5/ Id., p. 167.

Table VI B-6
United States Crude Oil
Reserves[1] by Leading Companies, 1981

Company	Reserves (million barrels)	Market Share (percent)
Sohio	3419	11.5
Exxon	2822	9.5
Arco	2549	8.6
Shell	2208	7.4
Amoco	1674	5.6
Getty	1322	4.4
Socal	1237	4.2
Texaco	1120	3.8
Mobil	898	3.0
Gulf	865	2.9
Sun	716	2.4
Marathon	641	2.2
Union	533	1.8
Phillips	476	1.6
Conoco (DuPont)	387	1.3
Cities Service	325	1.1
Subtotal	21,192	71.3
U.S. Total	29,785	100.0
Top 4	10,998	37.0
Top 8	16,351	55.0

Source: 1981 Annual Reports and 10k's.

1 Includes proven developed and undeveloped reserves of crude, condensate and leasehold natural gas liquids.

windfall profits tax can effect the way a major oil company decides to use its crude oil and can inhibit it from shipping crude to other companies, a factor which can also effect the geographic market.

An additional consideration in evaluating the apparent current policy of insisting on downstream divestitures but acquiescing in crude oil acquisitions is that the traditional remedy of divestiture may not lead to creating viable competitors from assets which are "spun off." The Texaco-Getty consent agreement, for example, requires that Texaco sell off refining pipeline and marketing assets within 12 months. If the consent agreement is finalized, the FTC can do its best to insure Texaco finds a buyer and that the divested assets will be used productively, but the FTC can't guarantee that result. In most antitrust cases, the divestiture remedy works reasonably well, but in a highly integrated industry, where established sources of supply may not be easily replaced, it is reasonable to be concerned about whether the assets Texaco sells off will be as productive as before.

Finally, the oil industry has been historically prone to collusion. As both the Justice Department merger guidelines and the FTC horizontal merger statement make clear, a relevant factor in assessing the likely impact of a merger is whether the unique characteristics of an industry make it more or less likely that outright agreements among competitors or coordinated behavior by

them, which restrain competition, will occur. The Commission's 1973 complaint against the major oil companies 6/ alleged a series of structural and conduct problems in the industry to be unfair methods of competition. When the Commission dismissed the complaint in 1981, it did so not on the grounds that the staff had failed to uncover any evidence to support these allegations but that the case had become too complex and bogged down to expect a resolution in the near future. In short, the Exxon case burst the seams of manageable litigation.

The fact that the Commission chose to end that case, with the express statement that "more focused proceedings" might be warranted, should not be taken to mean the oil industry is not an industry that warrants close scrutiny. It emphatically does. The degree of vertical integration, the ability of a few companies to influence supply and demand at one level of the system by controlling another level, the prevalence of exchange agreements, the frequency of joint ventures, the degree of information exchange, the pervasiveness of joint pipeline ownership, the tax incentives which encourage major companies to divert crude through their own vertically integrated operations, the incentives of the major companies to eliminate the independent sector of the industry, and the not infrequent historic examples of price-fixing in the past all suggest this

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6/ Exxon Corp., 98 FTC 453 (1981) (complaint dismissed).

industry is far from the textbook model. A simple assessment of horizontal market shares may miss the vast forest of potentially anticompetitive phenomena.

In summary, the evidence suggests two conclusions about antitrust concerns. First, antitrust problems can arise in the oil industry from crude oil acquisitions, even though horizontal concentration is not high, because of the problem of cutting off traditional sources of supplies to the independent sector. Second, the oil industry is not only massive in size but it is exceedingly complex. The industry is far from the textbook model and mergers, including those at the crude oil level, must often be assessed on a much more specific basis than worldwide or even domestic horizontal concentration.

Concerns outside Antitrust

The traditional concern of antitrust is competition within particular markets. It is quite clear that the Congressional intent which underlies the Sherman Act, the Clayton Act, the Cellar-Kefauver Antimerger Act, and the FTC Act is not limited to the economists' notion of efficient resource allocation. For example, our own FTC economists have declared that the FTC should be unconcerned about supracompetitive prices to consumers so long as they represent only "transfers of wealth" to merging firms or companies engaged in price-fixing. We should only bother ourselves, they say, with an actual loss in production and if we can't establish a substantial reduction, we have no business bringing an antitrust action. But the legislative history of the

antitrust laws shows clearly a Congressional concern about higher prices to consumers from anticompetive conduct. Similarly, the antitrust laws and court decisions interpreting them reflect a deep commitment to maintaining rivalry among diverse competitors, to preserving consumer choice, to protecting smaller competitors from unfair predatory behavior, and to avoiding undue concentrations of economic and political power. While it is difficult to apply some of these principles on a case-by-case basis -- and doing so would introduce too much subjectivity into antitrust enforcement and court decisions -- these values can and should be incorporated into general antitrust principles and rules.

On the other hand, some problems associated with business combinations fall outside traditional antitrust analysis. In particular, the diversion of capital investment from more productive uses, wasting financial and human resources in takeover fights, and tying up massive amounts of capital for acquisition do not fall into traditional antitrust analysis as applied by the Commission and the courts. Similarly, alleged "efficiencies" in production flowing from mergers have not been a traditional legal defense to a merger, primarily on the grounds that efficiency arguments are typically highly speculative and difficult to assess, although both the Justice Department and the FTC have stated that they will consider alleged efficiencies under some circumstances in exercising prosecutorial discretion. Chairman Miller of the FTC has argued that we should consider efficiencies to a much greater extent. The quarrel

between the White House and Mr. McGrath of the Justice Department over steel merger policy seems to be based, at least in part, on a disagreement about the steel companies' efficiency arguments. It may be that, if efficiencies are to be considered, antitrust analysis should be broadened to include those considerations mentioned above, a change which would certainly require legislation.

In any event, since concerns about capital investment and corporate waste are not traditional antitrust issues, the antitrust agencies will not take these factors into account in any direct way in deciding to challenge a particular merger. Consequently, if Congress believes there are significant problems that need to be addressed in this area -- and I believe there are -- legislation will be needed.

Do oil companies divert capital from exploration and other productive investment when they use billions of dollars in cash and credit to buy other firms? The answer is almost certainly yes. In lining up a credit line to buy Gulf, Mesa noted that its capital spending plans for 1984 had to be cut in half. Oil companies openly admit that they need new reserves and among the two choices -- drilling or buying another company -- merging is cheaper. Our staff found the exclusive motive for the Texaco-Getty acquistion was to gain control of Getty's crude oil.

Unlike an investment to build a factory, which is allocated to paying construction costs and buying machinery, the capital used to acquire a company is simply transferred to other hands and becomes available for investment. Thus, one can argue that

the $10 billion used to buy Getty will still be invested, if not in oil, than elsewhere in the economy. As Secretary Hodel argued: "That money doesn't disappear, it stays right in the economy." But a more important question, for purposes of assessing the long run productivity of the oil industry, is whether the likelihoood of investment in further exploration and development of oil is as high when windfall gains on oil stocks end up in the hands of individuals, institutions or other firms, particularly those outside the industry. I know of no definitive studies, but it is reasonable to assume that much less of this capital will go to such development. The firms likely to explore for oil are the firms which are committed to ths business of selling oil, not the individuals and institutions which profit from oil stocks shooting up. We should also recall that one of the arguments by the oil industry for decontrol of oil prices was that the industry needed incentives for developing new reserves, and one of the ironies of current policy is that companies are using profits from decontrol to buy the oil of their competitors.

There are other important issues outside of antitrust raised by big oil mergers, including the management resources wasted in takeover fights and the tying up of capital in lines of credit in preparation for takeovers which may or may not occur. We need to know more about these issues. In fact, one of the more troublesome aspects of the rush to merge is that the administration not only neglects antitrust enforcement but it shows a casual indifference to even studying the implications of the massive consolidations.

I believe there is ample justification for Congress to impose some temporary limitation on big oil mergers to enable Congress and the Executive Branch to gain understanding of this raging phenomenon. If these mergers really enhance productivity -- and are not merely a reaction to a window of opportunity caused by lax enforcement and depressed stock values -- a limited moratorium will only delay for a short time an industry restructuring which can continue to take place. But if, as seems more likely, these mergers promise only windfall profits to lucky shareholders and a device for eliminating the need to explore for oil by the majors, while threatening to reduce competition, Congress should act, and the sooner the better.

What type of legislation is warranted? I agree with the concept of a moratorium, but I would urge Congress to impose a moratorium that is long enough for serious study, long enough to insure that a useful and comprehensive analysis is undertaken rather than prompting executive branch agencies to defend the administration's policies under the guise of objective analysis. Consequently, I suggest that Congress create a national Commission to study both the antitrust and industrial policy ramifications of consolidations in the oil industry. The Commission could be made up of members appointed equally by the President, the House of Representatives and the Senate. Such a Commission should be allowed a reasonable period for a serious, comprehensive study -- a period which would necessarily require at least one year. Thus, a moratorium of eighteen months would be required to allow Congress the time to act.

> Some will argue that a moratorium of a year and a half on massive oil mergers is too long. But can one really argue that the American public will suffer from the loss of "efficiencies" -- now inchoate but promising to stimulate significant gains in productivity -- if this phenomenon is halted for this limited period. I submit that the productivity arguments are so speculative and the likelihood of lasting harm from the massive consolidations so high that the nation would be best served by a serious attempt to answer these crucial questions, before the damage becomes irremediable.

The CHAIRMAN. The distinguished Senator from Ohio.

Senator METZENBAUM. I have one question. Mr. Pertschuk, it has been said that existing antitrust laws, as enforced by the Federal Trade Commission, can adequately protect consumers from any problems caused by these oil mergers. You are a member of the Federal Trade Commission.

Looking at the facts, at the refusal of Reagan appointees to pursue antitrust violations, in connection with the Mobil-Marathon merger, and at the tentative approval of Texaco-Getty, would you tell us how secure we can be in relying on the current membership of the FTC to vigorously enforce the antitrust laws in this area?

Mr. PERTSCHUK. I do not believe that you can be secure at all, Senator Metzenbaum.

As you know, based upon the initial view of the evidence in the Texaco-Getty merger, and, of course, our consideration of the Mobil-Marathon proposed merger, I supported a preliminary injunction to halt those mergers. The Commission, while its staff found serious anticompetitive effects, was prepared to negotiate a consent agreement which, in my judgment and the judgment of others, did not provide the kind of security that you are seeking.

In addition to that, of course, there are external factors, which I outlined in my paper and which others have raised, which no Commission would be able to take into account as the antitrust laws are interpreted at this time.

Senator METZENBAUM. Thank you.

The CHAIRMAN. The distinguished Senator from Utah.

Senator HATCH. Mr. Pertschuk, I will ask you the same question I asked Senator Rudman, I believe, and that is: do you know of any reason why the Mobil-Superior and Gulf-Socal mergers should not be judged the same way that the Texaco-Getty merger is judged? Or is there any reason to have a different standard for Texaco-Getty than for these that would be affected by this particular interjection of legislation into the process?

Mr. PERTSCHUK. Well, Senator, I think my answer is slightly different than Senator Rudman's.

I consider that the standards have been changed by administrative fiat. The fact of the matter is that none of these mergers would have been contemplated as late as 5 years ago.

Senator HATCH. Well, let's see if I understand that. You are saying the antitrust laws are embracive enough to resolve these merger problems?

Mr. PERTSCHUK. Some.

Senator HATCH. Some of the problems. But you are not sure they are being applied by this administration or by the Justice Department as presently constituted.

Mr. PERTSCHUK. I am sure they are not, yes, sir.

Senator HATCH. I see. Would you be the majority view on the Federal Trade Commission or the minority?

Mr. PERTSCHUK. I certainly do not represent the Federal Trade Commission nor any of its majority members at this proceeding.

Senator HATCH. So your viewpoint would be the minority view on the Commission?

Mr. PERTSCHUK. My view is decidedly the minority view, yes, sir.

Senator HATCH. That's all.

The CHAIRMAN. Senator Johnston, do you want to ask any questions?

Senator JOHNSTON. No, sir

The CHAIRMAN. Senator Nickles.

Senator NICKLES. Mr. Chairman, just a real quick question.

You mention that you represent the majority view on the Commission?

Mr. PERTSCHUK. No; the minority, sir—at this time. [Laughter.]

Senator NICKLES. There are five Commissioners. Were you the lone dissenter on the Texaco-Getty vote?

Mr. PERTSCHUK. Yes, sir.

Senator NICKLES. One other question. Most people were aware of the Getty debate for a long time, the fact that some of the Getty members wanted to sell.

Do you think they shouldn't have been able to sell their stock?

Mr. PERTSCHUK. Shouldn't have been able to sell their stock to anyone? No; I certainly don't take that position. I approached the facts of the Texaco-Getty acquisition under the law, as I saw it; and that particular transaction seemed to me, on the basis of the evidence, to appear to violate the antitrust laws, which would mean the Getty family would not sell their stock to Texaco.

Senator NICKLES. Their stock value being so large and the assets that it represented being so large—it would take a large company to be able to buy that stock. I don't know that you could ever satisfy your desires to not have a merger and the Gettys could be held hostage as far as ever being able to move that stock.

Mr. PERTSCHUK. I would like to be in their position, Senator, but I am afraid I cannot offer counsel on how otherwise they could dispose of their stock. I suspect they can and still meet the terms of the proposed moratorium.

They certainly could dispose of their stock and meet the requirements of the antitrust law, that I am confident of.

Senator NICKLES. You were the lone dissenter on that consent agreement?

Mr. PERTSCHUK. Yes, sir.

Senator NICKLES. Just one other comment, a lot of people are interested in the consent agreement. I am concerned about the part of the consent agreement that is forcing—just so you will know that some of us read these consent agreements, and we are bothered by the Commission's action—in some cases successful organizations to spinoff marketing and refining assets one at a time that the market is soft, which sometimes can cause a real disruption of employees and the numbers of jobs available.

Mr. PERTSCHUK. Senator, I share that concern. I was surprised that this Commission adopted what is really a highly regulatory approach in negotiating the Texaco-Getty consent agreement, which does involve the Commission supervising the activities of the merged Texaco-Getty corporation and supervise a number of discrete parts of the sale.

It seemed to me the simplest and most efficient way was to stop the transaction altogether.

Senator NICKLES. Or, if you are going to allow the transaction to go through, allow it to go through whole and not force major segments of the corporation to be dismembered.

Thank you, Mr. Chairman.

The CHAIRMAN. The distinguished Senator from Alabama.

Senator HEFLIN. Mr. Pertschuk, you state you support this bill.

Mr. PERTSCHUK. Yes, Senator, in its major outlines.

Senator HEFLIN. And you think the reporting requirements are adequate?

Mr. PERTSCHUK. Actually, Senator, I would have preferred to see a longer period of time elapse. I had suggested in my testimony an 18-month moratorium with a 1-year study, and I do that because I think that the questions raised, the fundamental questions raised by the sponsors of the legislation, have not really been answered. All week long we have heard nothing but speculation in the press about whether or not capital is truly diverted from exploratory uses, where the money goes. No one seems to know where the money goes when these amounts of capital are employed, and whether or not the money ends up in productive investment or not.

I think the sponsors of the legislation can point to serious diversions of capital and the threat of diversions of capital; but I think the study should encompass some good, hard case studies of past mergers and what happened.

And I don't think we have that information in hand, although I think 6 months would give us a strong leg up on a picture of the radically restructuring industry, so it is certainly worthwhile to have 6 months.

Senator HEFLIN. Do you think there should be any additional reporting agencies?

Mr. PERTSCHUK. Reporting agencies, sir?

Senator HEFLIN. Yes.

Mr. PERTSCHUK. I think that the concept of the Commission or the advisory committee—rather than individual executive or independent regulatory agencies reporting—makes a lot of sense, because it can be done quickly and can be independent of the administrations position. That Commission, in turn, can request, under the usual procedures of congressionally authorized investigations,

from any agency possessing any expertise, precisely the information it needs.

And I think it should have those powers.

Senator HEFLIN. You don't suggest any additional amendments to the bill?

Mr. PERTSCHUK. No, sir.

Senator HEFLIN. Well, I am looking at the five reporting agencies, the Federal Trade Commission. I suppose, if you are in a minority, you could file a dissenting report from the report.

Mr. PERTSCHUK. Certainly; but actually we do have expertise at the Commission. We have good staff who know this industry and who can guide the work of Congress in judging its implications, yes, sir.

Senator HEFLIN. The Attorney General is an appointee of the administration. Do you suppose there would be an opportunity for a dissenting report there?

Mr. PERTSCHUK. Not likely.

Senator HEFLIN. I suppose the Secretary of the Treasury is an appointee of the administration, and there wouldn't be an opportunity for a dissenting report there, would there?

[Mr. Pertschuk shakes head no.]

Then the Secretary of the Interior is an appointee of the administration. There wouldn't be any dissenting report filed there, would there?

Mr. PERTSCHUK. No, sir.

Senator HEFLIN. The Administrator of the Energy Information Administration, I believe he is an appointee of the administration.

Mr. PERTSCHUK. Well, but, of course, he has in hand substantial important objective data which would be important for the Commission regardless of the gloss and evaluation that the Secretary placed on that data, so that I think information, objective information, would be available from the agencies for the study.

Senator JOHNSTON. Would the Senator yield for a moment?

Senator HEFLIN. Please let me finish my line of questions.

So basically what you are asking for is the position of the administration. We have spent the last 6 months to determine what the position of the administration is.

Don't we already know that?

Mr. PERTSCHUK. I don't think that is the thrust of the legislation.

Senator HEFLIN. It's a moratorium for study, and the legislation, as I see it, has got five. Who are your additional?

Senator JOHNSTON. If the Senator would yield, the present Commission is only a model of the Lennows Commission. The four members are selected two each by the Speaker of the House, by the minority leader; two in the same method by the majority leader and minority leader of the Senate; one by the President.

That Commission would then report to the Congress on the various issues, such as concentration, competition, the effect on exploration, effect on Federal revenues, the capacity to develop oil and gas resources. And it would also mandate that the various Federal commissions would be required to cooperate with this Commission—it would mandate the FTC, the Department of Justice, Treasury, et cetera, to cooperate with them

I think that model is a better one than the initial legislation.

So that will be in our amendment, that kind of commission.

Senator HEFLIN. You mean they won't have these reporting requirements?

Senator JOHNSTON. No; the reporting requirements are not there; the Commission will be required to report to the Congress its facts and conclusions.

The idea here, it is as much to get information on factual matters like, for example, what would be the effect on the revenues of the country, as it would be to come to a conclusion.

The CHAIRMAN. Any other questions?

If not, the witness is excused.

Mr. PERTSCHUK. Thank you very much, Mr. Chairman.

The CHAIRMAN. The next witness is the Honorable Timothy J. Muris, the Director of the Bureau of Competition, Federal Trade Commission.

Come around, Mr. Muris.

Mr. Muris, do you have a written statement?

Mr. MURIS. Yes, sir.

The CHAIRMAN. Would it suit you to put it in the record and summarize it in 5 minutes?

Mr. MURIS. Yes, sir.

The CHAIRMAN. This light here is green; when it turns red, your time is up.

STATEMENT OF HON. TIMOTHY J. MURIS, DIRECTOR, BUREAU OF COMPETITION, FEDERAL TRADE COMMISSION, ACCOMPANIED BY RON ROWE, PETROLEUM OFFICE

Mr. MURIS. Yes, sir. With me is Ron Rowe who is the head of our Petroleum Office.

Let me just briefly make three points. I want to discuss our oil merger study, our case enforcement, and a few general points about the crude oil market.

In response to a congressional request, the Commission directed its petroleum industry experts to conduct an in-depth, exhaustive review of numerous issues involved in petroleum industry acquisitions. Just 18 months ago, the Commission forwarded to Congress its 300-page report. The study concluded, among other things, that, first, petroleum mergers occur for a variety of reasons, including wider use of enhanced oil recovery techniques, divergent expectations concerning future crude oil price movements, the phased decontrol of crude oil, and various tax reasons.

Second, the Commission concluded that it did not believe that acquisitions occurring in the period studied adversely affected petroleum prices or availability of supply. Third, the study found no evidence that increased oil merger activity significantly diverted capital from exploration and development. Indeed, the study found that crude oil exploration and production generally increased during the period of increased oil merger activity.

Fourth, the Commission concluded that most geographic markets at the various levels of the petroleum industry were not highly concentrated, that mergers generally increased concentration levels only slightly, and that such increases did not appear to have endangered the substantial competition the Commission found to

exist. Finally, the Commission recommended against any legislative ban on petroleum mergers.

Turning to specific cases, in the last 2½ years, the Commission has investigated three such cases—Mobil-Marathon, Gulf-Cities Service, and Texaco-Getty.

In each case, I think it should be emphasized, the Commission took enforcement action. However, none of the competition problems that we found were caused by or even related to the overall size of the companies that would have been created. Each of the problems affected only a relatively small, identifiable region of the country. Further, each problem pertained only to one or, at most, a few of the numerous product marketed by a large integrated oil company. Finally, none of the mergers created an antitrust problem involving the discovery and production of crude oil.

The Texaco merger was different than the other two in one crecial aspect: Texaco was willing to cure the problem. When firms are willing to cooperate, the standard practice of the Federal Trade Commission has always—and I repeat always—been to attempt to obtain by means of a consent agreement the relief necessary to remedy the perceived problem.

And in fact we believe, at the staff level, that we did that in this case. We required, for example, Texaco to divest its Eagle Point refinery in New Jersey, we required that they sell some 1,900 retail gas stations, we required divestiture of a pipeline, refinery, and related assets in Colorado, Kansas, and other parts of the country in that area, and we required Texaco to continue to sell so-called heavy crude oil to California independents.

Thus, the idea that the Commission is not willing to act, and has not acted, is erroneous. Indeed, the total cost of the assets Texaco is ordered to divest runs into several hundreds of millions, which does not include the nearly $3 billion of crude oil that Texaco will be forced to sell.

Part of the reason there has been some criticism or allegations that the Commission has not enforced the law in regards to these mergers is that there is a fundamental misunderstanding of the nature of competition in crude oil. If you turn to tables 1 and 2 of my testimony, you will see that crude oil, using the United States as a national market, is very unconcentrated. In fact, if you use the 1968 merger guidelines, which have everywhere been recognized to be too stringent and have been repudiated, including by Commissioner Pertschuk and all the members of the Commission, none of the mergers that have thus far come before the Commission would have been challenged merely on the basis of the crude oil acquired. Under the more superior and more up-to-date 1982 guidelines, those mergers for sure would not have been challenged

Let me make one last point in terms of the allegations of Commissioner Pertschuk. I think he has fundamentally mislead you about what the Commission did in regards to Mobil-Marathon—and I notice that Senator Metzenbaum said the Commission did not act. In fact, the Commission did file a preliminary injunction, and in fact one of the bases of that preliminary injunction was that Marathon would have been removed as a unique source to supply independents. And the Commission was not willing to allow the merger, unless Mobil could convince us that they could correct the

situation by creating another company that would have been able to take care of those independents.

The CHAIRMAN. Thank you. The distinguished Senator from Ohio.

Senator METZENBAUM. I have no questions.

The CHAIRMAN. The distinguished Senator from Utah.

Senator HATCH. I just have a couple of questions for you.

Mr. Muris, in yesterday's Washington Post, Paul Samuelson argued that our tax laws are the real cause of the current merger activity, and, further, that the existing antitrust laws are adequate to correct potential problems of concentration.

Do you agree or disagree with Mr. Samuelson's conclusions?

Mr. MURIS. I agree that from a competitive standpoint the existing antitrust laws are adequate, but, quite frankly, speaking personally and not in terms of antitrust, as one who cares about the efficient allocation of resources and the effect on consumers, the tax laws no doubt have perverse effects.

Senator HATCH. Then you agree with him?

Mr. MURIS. I don't know that I agree in every particular.

Senator HATCH. No, but I am saying with those two conclusions.

Mr. MURIS. He asserted in essence that the sole purpose of these mergers was for tax reasons and I am not convinced that is true.

Senator HATCH. Mr. Pertschuk indicated that the problem here is lax antitrust enforcement by the administration. I am kind of the opinion that the problem here, or at least the merger between Socal and Gulf, has been triggered by undervalued stock.

Am I off base there, am I wrong?

Mr. MURIS. Well, it really is our policy not to comment on merger matters before us.

Senator HATCH. Well, I will relieve you of commenting, then.

Has the FTC's experience under the 1982 guidelines indicated any particular areas where revision is desirable or necessary, and will any of these areas be applied to the Gulf-Socal merger, the Mobil-Superior merger? Were any of these problem areas applied to the Texaco-Getty merger?

Mr. MURIS. Again, referring in general to the antitrust laws as they apply to oil acquisitions, without referring to specific cases that we haven't ruled on, the laws are indeed adequate to protect consumers. The changes that were made in 1982, which Commissioner Pertschuk and all the Commissioners agreed with, are changes that are good. Even under the old standards, however, which the courts have changed, in terms of crude oil production, the mergers that we have looked at so far would not have been attacked.

Senator HATCH. Just one last question, which I have asked other witnesses. Do you know of any reason why the Mobil-Superior and Gulf-Socal mergers should not be judged according to the same standards as the Texaco-Getty merger?

Mr. MURIS. We will apply the same general antitrust standards to all mergers, again without commenting specifically on the facts of the two matters before us, which we have not had a chance to evaluate.

Senator HATCH. But you will have to admit that if this legislation passes, the same standards will not be applied or applicable.

Mr. MURIS. Yes; and I think that this moratorium legislation has serious problems. The Commission opposed this sort of legislation before, and I think it is not a good step at this time.

Senator HATCH. Thank you, Mr. Chairman.

The CHAIRMAN. Thank you. Senator, do you have any questions? We are anxious to move on.

Senator JOHNSTON. Yes, just very quickly. The charter of the FTC deals with competition and concentration, and you do not deal with such things as the advisability of tax policy or energy policy, am I correct on that?

Mr. MURIS. Yes, sir.

Senator JOHNSTON. You do see some perverse effects in the tax laws, did you say, on these mergers?

Mr. MURIS. I was not referring specifically to these mergers, but I do think that when people engage in transactions solely for tax reasons and not reasons that are related to efficiently moving resources, that that is a problem. And the reason it is a problem is that in any kind of this transaction there is a lot of money spent on lawyers, on accountants, and financial experts, and that if those expenses are made solely for tax reasons, is a problem.

But the solution seems to me to change the tax laws.

Senator JOHNSTON. You would say that the three pending mergers are for that very effect, and you can recite the figures, I guess, as to how much it is going for—arbitrageurs, tax lawyers, et cetera.

Mr. MURIS. Well, the actual percentage that goes for the transaction cost is very small; it is less than 1 percent of the total value of the merger. I am not asserting that without the tax laws these mergers would not occur, but I am suggesting that if we do have problems, the problems do appear to be in the tax laws.

Senator JOHNSTON. It is a perverse effect, I think were your words.

Mr. MURIS. Yes.

Senator JOHNSTON. Thank you

The CHAIRMAN. Thank you. The distinguished Senator from Alabama.

Senator HEFLIN. I was told that in the Texaco-Getty merger, the combined reserves of domestic oil in the United States did not exceed 5 percent of the total reserves domestically in the country, is that approximately right?

Mr. MURIS. Yes, sir.

Senator HEFLIN. Will the proposed mergers, after they take place, exceed more than 7 or 8 percent in any one merger?

Mr. MURIS. In terms of reserves, using the United States as a geographic market, the answer is no.

Senator HEFLIN. In other words, even if all of these mergers go through, there would be no concentration of reserves in the United States to exceed 10 percent?

Mr. MURIS. Not based on the latest figures that we have, which are 1982 figures.

Senator HEFLIN. Are there other areas of business in which the concentration of the market will far exceed the 10-percent concentration, like automobiles or other areas?

Mr. MURIS. In terms of crude oil production and crude oil reserves, of all our major industries, this is one of the least concen-

trated. But when you move downstream into refining, pipelines, and wholesale terminals, and gas stations, then there can be some serious anticompetitive problems. In all three of the cases before the Commission, the Commission moved to try to prevent and eliminate those problems.

Senator HEFLIN. And in each one—you have taken steps to prevent any excessive concentration?

Mr. MURIS. Yes, sir.

Senator HEFLIN. Of segments at certain stages?

Mr. MURIS. Yes, sir.

Senator HEFLIN. If Congress were to try to enact laws pertaining to one industry, does that raise any particular constitutional issue of spotlighting one area and leaving the rest of the issues in an unequal status?

Mr. MURIS. I am not a constitutional scholar, sir, so I hesitate to answer that question. I do not know for sure.

Senator HEFLIN. But under the present law, the Federal Trade Commission is charged with standards and criteria to prevent anticompetitive results from occurring in acquisitions and in mergers. Is that one of the responsibilities of the Federal Trade Commission?

Mr. MURIS. Yes, sir. And we, in fact, are vigorously enforcing those laws. We filed a preliminary injunction last week, and, at the moment, we have two more preliminary injunction recommendations before the Commission.

Senator HEFLIN. That's all.

The CHAIRMAN. Thank you, Senator.

Senator Nickles, do you have any questions?

Senator NICKLES. No, Mr. Chairman.

The CHAIRMAN. Thank you very much for your presence and for your testimony.

Mr. MURIS. Thank you.

[Prepared statement and letter follows:]

PREPARED STATEMENT

OF

TIMOTHY J. MURIS*
DIRECTOR
BUREAU OF COMPETITION

FEDERAL TRADE COMMISSION

BEFORE THE

COMMITTEE OF THE JUDICIARY

UNITED STATES SENATE

March 15, 1984

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* The opinions expressed are solely those of the author and do not necessarily reflect the views of the Federal Trade Commission or any individual Commissioner.

Mr. Chairman and Members of the Committee: I appreciate the invitation to appear before the Committee today to discuss the important and timely issue of mergers in the petroleum industry. As Director of the Federal Trade Commission's Bureau of Competition, my focus will be upon the antitrust implications of petroleum mergers and acquisitions, that is, their effect upon competition and the price and availability of petroleum products for the American consumer. The views I will present are those of the Bureau of Competition, and do not necessarily represent those of the Commission or of any individual Commissioner.

A substantial portion of the FTC's antitrust work involves reviewing corporate mergers and acquisitions* to assure they do not violate federal antitrust laws. The FTC's Bureaus of Competition and Economics have developed considerable expertise in analyzing competition issues involving the petroleum industry. The Bureau of Competition, for example, has for several years maintained a separate Petroleum Division, consisting of antitrust attorneys and other professionals who specialize in analyzing competition issues in the petroleum industry. The agency's staff has developed its expertise over many years, in several cases and investigations. These matters include the Commission's Exxon case against the major petroleum companies (dismissed in 1981) and the oil company mergers that have occurred over the past few years.

Given this considerable petroleum industry experience, it is not surprising that the Commission is performing the government's antitrust review of the current oil mergers -- Texaco/Getty, Socal/Gulf, and Mobil/Superior. As the Committee is aware, the Commission has provisionally accepted a consent agreement remedying potential antitrust concerns raised in the Texaco matter. The Commission's proposed remedy is now on the public record, and interested persons will have until May 7 to file written comments. The Commission has only just begun its review of the proposed Socal and Mobil transactions, however. Therefore, it is premature to attempt any detailed discussion of those mergers' likely impact. I will, nevertheless, be happy to discuss both the procedures the Commission is using to review those mergers and the antitrust concepts relevant to petroleum mergers in general.

In this testimony, I first discuss our 1982 study of oil mergers, one of the most detailed and comprehensive studies published on the subject. I next evaluate our past enforcement regarding oil mergers, in particular the recent provisionally accepted consent agreement in the Texaco/Getty matter. Finally, I discuss briefly the issue of increased concentration in production of crude oil.

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* As a convenient shorthand, I will henceforth refer only to "mergers."

I. The 1982 Petroleum Merger Study

In January, 1982, eight congressional leaders from both houses of Congress asked the Commission to investigate the impact of mergers and acquisitions involving large petroleum companies. In response to this request, the Commission directed its petroleum industry experts to conduct an in-depth, exhaustive review of numerous issues involved in petroleum industry acquisitions. Just 18 months ago, in September 1982, the Commission forwarded to Congress its 300-page report entitled, "Mergers in the Petroleum Industry," presenting its analysis and conclusions.[1] This "Oil Merger Study" reached a number of significant conclusions regarding oil mergers that are relevant to the issues before this Committee. It may therefore be helpful to summarize these conclusions.

First, oil industry acquisition activity did increase during the 1979-1980 period studied, although a few large transactions accounted for much of the increase. (As I discuss below, heightened activity has again resurfaced in recent months.) Second, petroleum mergers occur for a variety of reasons, including: wider use of enhanced oil recovery techniques; divergent expectations concerning future crude oil price movements; the phased decontrol of crude oil; the imposition of the windfall profits tax; and corporate income tax provisions such as those permitting an increased basis of acquired assets, and redepreciation of assets for tax purposes.

Third, the Commission concluded in the Oil Merger Study that it did not believe that acquisitions occurring in the period studied adversely affected petroleum product prices or availability of supply. Fourth, the Oil Merger Study found no substantial evidence that increased oil merger activity significantly diverted capital from exploration and development of energy sources. Indeed, the Study found that crude oil exploration and production generally increased during the period of increased oil merger activity. (Of course, we will continue to study this and other issues as we evaluate current merger activity.) Fifth, the Commission concluded that most geographic markets at the various levels of the petroleum industry were not highly concentrated; that mergers generally increased concentration levels only slightly; and that such increases did not appear to have endangered the substantial competition the Commission found to exist in most aspects of the petroleum industry.

The remaining conclusions of the Oil Merger Study appear especially relevant to the Committee's deliberations. The Commission concluded, sixth, that transaction costs -- including investment banking and legal fees -- for most petroleum acquisitions ranged from one-half of one percent to one percent (and in some cases exceeded one percent) of the total purchase price. Seventh, the Commission identified several possible

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[1] Commissioners Pertschuk and Bailey attached a separate statement to the report noting that they did not agree with all the conclusions reached in the report.

efficiencies that resulted from some petroleum mergers. These include application of technical know-how to increase crude oil production and benefits flowing from revaluations of crude oil reserves.

Finally -- and perhaps most pertinent for the Committee's present deliberations -- the Commission recommended against any legislative ban on oil company mergers. The Commission concluded that:

> Such interference in normal market forces is unwarranted, both because there have been no significant adverse implications on the state of competition in the industry from mergers, and because mergers with significant competitive impact can be satisfactorily examined under Section 7 of the Clayton Act and the 1976 Hart-Scott-Rodino amendments to that statute.[2]

With this Study as a general framework, I will now turn to a brief summary of the Commission's recent investigative and enforcement actions involving petroleum industry mergers. Such a summary is useful to place the current merger activity in context.

II. Recent FTC Actions Against Petroleum Mergers

A. Mobil/Marathon

Perhaps the logical starting point is Mobil's unsuccessful attempt in late 1981 to acquire Marathon. As the Committee will recall, that bid followed an earlier unsuccessful attempt by Mobil to acquire Conoco, which instead became a DuPont subsidiary. The FTC's investigation of the proposed Mobil/Marathon merger revealed significant potential antitrust concerns involving competition in certain "downstream" markets -- those involving the wholesale and retail distribution of gasoline, home heating oil, and certain other petroleum products. The Commission determined that these concerns were too significant to permit the merger to proceed, and filed a preliminary injunction suit to block the merger.

It is useful here to correct a common misconception about the FTC's enforcement action in the Mobil/Marathon case. Some have said that it was a private antitrust suit by Marathon that blocked Mobil's takeover bid, and that the FTC's subsequent action was too tardy and had no effect. Yet, the FTC utilized all of the statutory time period permitted under the Hart-Scott-Rodino premerger notification procedures to allow for an analysis

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2 See FTC Report "Mergers in the Petroleum Industry," supra, at 298.

as thorough and as focused as possible. I have always been puzzled that some have argued the Commission should have rushed its analysis simply because private litigation was initiated. Sound federal antitrust policy dictates that enforcement decisions of federal antitrust authorities be governed by the evidence and the law, not by the sometimes frantic legal maneuvers of firms involved in takeover contests.

Marathon's private suit certainly played a major role in the eventual success of U.S. Steel in acquiring Marathon. The Commission, however, was ready, willing, and able to litigate its preliminary injunction suit had that proven necessary to prevent the anticompetitive aspects of Mobil's proposed acquisition of Marathon.

B. Gulf/Cities Services

The next major Commission action involving this industry occurred when Gulf Oil Company attempted to acquire Cities Services Company in mid 1982. Once again, the FTC conducted its review under the Hart-Scott-Rodino procedures, and once again the Commission determined that enforcement action was required to forestall anticompetitive consequences. Following the Commission's filing of a preliminary injunction suit, Gulf abandoned its bid to acquire Cities Services. Occidental Petroleum Company -- also one of the smaller, "second-tier" oil companies -- subsequently acquired Cities Services. The FTC closely reviewed that merger as well, concluding it presented no danger of any substantial lessening of competition.

C. Texaco/Getty

The Texaco/Getty merger followed the pattern of the prior two transactions: a "major," vertically-integrated petroleum company attempting to acquire a smaller, second-tier firm, primarily to gain control over the latter's crude oil reserves. And, the FTC once again concluded that the proposed merger raised substantial antitrust concerns warranting enforcement action. (I should note here that, in contrast to the Mobil/Marathon case, two private antitrust suits failed to block the merger on antitrust grounds.)

The Commission's expertise in the petroleum industry enabled it promptly to pinpoint four antitrust problems. First, the merger raised concerns about competition in the manufacture and transportation of "refined light products" in the northeastern United States. These products include gasoline, fuel oil, jet fuel, and kerosene. Second, the merger threatened to reduce competition in the wholesale distribution of gasoline, home heating oil, and diesel fuel to retailers in the Northeast. Third, the Texaco/Getty combination raised a danger of diminished competition in transporting refined light products by pipeline into Colorado. Finally, the merger might result in the demise of

independent refiners in California, reducing competition in the already moderately concentrated California refinery market.

Several crucial facts can be gleaned from close scrutiny of these potential antitrust problems: First, none of the competition problems are caused by, or even related to, the overall size of the oil company created by combining Texaco and Getty. Second, each of the problems affects only a relatively small, identifiable region of the country. Third, each problem pertains only to one or at most a few of the numerous products marketed by a large, integrated oil company. Fourth, the Texaco/Getty merger created no antitrust problem involving the discovery and production of crude oil.[3]

The four antitrust concerns identified were serious ones. The Commission's staff of economists and lawyers, however, unanimously concluded that they could be remedied without barring the entire merger. Texaco, for its part, was willing to do so. It is important here to stress two points: first, firms proposing to engage in potentially anticompetitive acquisitions are not always cooperative in working with the Commission to alleviate competitive problems; and second, when such firms are willing to cooperate, our standard practice has always been to attempt to obtain by means of a consent agreement the relief necessary to remedy the perceived antitrust problems.

Thus, following our standard practice in merger investigations, we entered a series of intensive negotiations with counsel for Texaco to determine whether the antitrust concerns could be eliminated. As a predicate for any possible settlement of the antitrust issues, we insisted upon a signed agreement obligating Texaco to maintain Getty as a separate, viable oil concern throughout the public comment period while the Commission assessed whether to give final approval to any consent agreement that was reached. When Texaco agreed to this precondition, negotiations continued on the question of remedying the antitrust concerns.

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[3] The California problem did not concern the discovery and production of crude oil, even if California is treated as a separate geographic market. Instead, the potential competitive problem we found related to refiners who had built plants designed to use the cheaper, "heavy" crude oil that Getty sold. Although these refineries produce the same products as do refineries using lighter crude, the cost of retooling the refineries to rely on more-expensive, lighter crude is so high that loss of a reliable source of heavy crude over the mid-term (three to five years) could lead to their departure from the market.

Following these negotiations, Texaco agreed to submit to an FTC order that the agency's staff of economists and attorneys unanimously agreed would remedy any possible anticompetitive harm from the merger. As the Committee is aware, a four-member majority of the Commission provisionally accepted that consent agreement on February 13, 1984.

With your permission, I will submit for the record a copy of that consent agreement, together with a copy of the proposed complaint setting forth the Commission's allegations of competitive harm, the hold separate agreement signed by Texaco, and a detailed staff analysis of the antitrust concerns and the relief the Commission obtained.

D. The Texaco/Getty Consent Order

The relief in the consent agreement addresses each of the four potential competitive concerns outlined above. It does so in a precise, focused manner: the Commission's knowledge of the industry enabled it to cut with a scalpel, not a meat cleaver. At the same time, the relief adequately addresses all of the competitive concerns. Both of these propositions are readily apparent from a brief summary of that relief.

To remedy any possible increased incentive Texaco might have to restrict the output of refined light products available in the Northeast, the order requires Texaco to take two signficant steps. First, it must divest its Eagle Point, New Jersey refinery to a buyer approved by the FTC. The Commission will review proposed buyers to assure they can operate the refinery as a competitive facility likely to remain in the market. Second, for ten years Texaco must always vote in favor of proposals to expand the Colonial Pipeline. Along with other petroleum firms, Texaco is a co-owner of Colonial, which transports refined products from the Gulf Coast through the Southeast and into the Northeast. These two provisions, working together, will diminish the possibility of supply restrictions in the Northeast.

In addition, the Commission's order requires Texaco to divest its wholesale gasoline terminal operations in six Northeast areas (and a seventh in Colorado). To assure that Texaco could make an adequate divestiture of the wholesale terminals, the order also requires Texaco to divest some 1900 retail gasoline stations that the wholesale terminals supply. Once again, the Commission must approve in advance the buyers of these properties.

This last point merits some elaboration. It is true that Texaco -- on its own initiative and without consultation with the Commission or its staff -- has entered a contract to sell these Northeast wholesale and retail properties to an independent gasoline marketer operating under the "PowerTest" name. Texaco entered this contract in part to reduce its antitrust exposure in a private (and unsuccessful) antitrust suit brought by Pennzoil

to block the acquisition of Getty. The Commission has not approved PowerTest -- or anyone else -- as a buyer of any of the acquired Getty assets. After the Commission gives final approval to the consent agreement, Texaco will be required to submit proposed buyers for FTC approval. Interested persons will then have a 30-day public comment period to submit written comments on the question of whether PowerTest or any other proposed buyer should be approved. Among the factors the Commission will consider is whether the buyer is willing and able to maintain the assets as viable properties in competition with those of existing firms. As with other properties to be divested, the Commission will insist upon adequate assurances that the properties will remain competitive.

The third principal provision of the consent agreement requires Texaco to divest Getty's substantial ownership interest in the Chase pipeline, which is one of four pipelines that delivers refined light products into the Denver, Colorado area. Texaco already owns a portion of another of those pipelines, raising an obvious antitrust concern. To prevent Texaco from using its partial control over two of the four pipelines to raise prices to consumers in Colorado, the Commission required Texaco to shed its interest in the Chase pipeline. The pipeline probably could not be sold by itself, however, because it is only valuable in conjunction with the Eldorado, Kansas refinery to which it is connected and which supplies the products shipped to Colorado. Again for the sole purpose of assuring that adequate divestiture could be accomplished, the Commission elected to take the prudent enforcement approach and to also require divestiture of the Eldorado refinery and the associated assets necessary to operate it and supply it with crude oil.

We will pay close attention to the question of whether a proposed buyer of the Eldorado refinery will be willing and able to operate it successfully so that it adds competition to the marketplace, while simultaneously maintaining productive employment for Kansans. In this regard, one factor of particular interest will be whether the buyer will be able to obtain the necessary supply of crude oil to operate the refinery. The Commission's requirement that Texaco sell crude oil gathering pipelines running from crude oil fields to the Eldorado refinery should go far to assure that goal.

The final substantive order provision requires Texaco to continue to sell so-called "heavy" crude oil to independent California refiners that bought from Getty prior to its merger into Texaco. Those refiners have in many cases made costly adjustments to their refineries to process this unique type of crude oil. The merger raises a concern whether such refiners can continue to obtain a crude supply, because Texaco may have tax incentives, unrelated to the efficient use of the resources involved, to use heavy crude oil in its own West Coast refineries. Such a shift could weaken competition from independent refiners, and might even cause some to leave the

market. To prevent such problems, the consent order requires Texaco to continue supplying those current Getty refiner-customers for a 5-year period. By that time offshore sources of heavy crude oil already discovered would be more than ample to eliminate any supply problems the merger might create for independent refiners.

Although the total cost of the assets Texaco is ordered to divest is small relative to the total $10.1 billion cost of the acquisition, it is nonetheless substantial -- running into several hundreds of millions of dollars. (The precise cost of the to-be-divested assets is of course uncertain, because potential buyers need not be arranged until after the Commission gives final acceptance to the consent order.) Further, the Commission's staff estimates that the value of the crude oil Texaco is required to sell to certain independent California refiners will exceed $3 billion over the 5 years the supply obligation will be in place. By any measure, the magnitude of this relief is substantial.

E. Conclusion Regarding FTC Enforcement

Thus, in each of the proposed mergers involving attempted takeovers by a "major" oil company of a second-tier oil company, the FTC pursued enforcement action. Some have apparently forgotten these vigorous actions. Thus, one hears cries that the Commission's allegedly "lax" merger enforcement policy was somehow a driving force behind the latest "big oil" mergers. As noted, the facts belie such claims. If there was a message to be drawn from prior FTC actions, it was that mergers between competing oil concerns would be subjected to rigorous antitrust scrutiny and, if antitrust concerns were found, would be challenged.

Some of the criticism may be due to a fundamental misunderstanding of the competitive nature of the oil industry, particularly at the level of crude oil production. I turn next to this issue.

III. Increased Crude Oil Concentration

One of the most frequent concerns that has been raised in recent days regarding petroleum industry mergers is that they are concentrating the ownership of United States crude oil reserves in the hands of a very few large oil companies. Such concentration is dangerous, it is said, to consumers.

It is useful to step back and place these assertions in perspective. The Commission's 1982 Oil Merger Study concluded, for instance, that the petroleum industry in general -- and the production of crude oil in particular -- is relatively unconcentrated. This conclusion is borne out when one analyzes how mergers involving crude oil reserves have historically been

treated under the federal government's merger enforcement guidelines.

A. The 1982 Guidelines

In each of the major oil company mergers it has analyzed in the past few years, the Commission has applied the analytical approach detailed in the Commission's 1982 "Statement on Horizontal Mergers" and in the Justice Department's 1982 Merger Guidelines. These guidelines make clear that concentration is a necessary but not sufficient condition before the government will attack a merger. Unless certain specified levels of concentration are reached, the conditions for non-competitive performance in an industry are unlikely to exist. Although there may be a few special problems in crude oil,[4] in general, the concentration level is very low in crude oil. Tables 1 and 2 provide the latest available statistics for crude oil production and reserves in the United States.

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[4] See FTC Report "Mergers in the Petroleum Industry", supra, at 151-54.

TABLE 1

U.S. CRUDE OIL, CONDENSATE AND NATURAL GAS LIQUIDS PRODUCTION, 1982
(000 Barrels/day)

Company	Production	Percent of Total
Exxon	740.0	7.3
Standard of Ohio	694.9	6.8
Atlantic Richfield	607.4	6.0
Shell	519.0	5.1
Standard of Indiana	409.0	4.0
Texaco	352.0	3.5
Standard of California	332.0	3.3
Gulf	328.7	3.2
Mobil	309.0	3.0
Getty	280.0	2.7
Phillips	260.0	2.5
Sun	212.1	2.1
Union	171.4	1.7
Marathon (U.S. Steel)	160.1	1.6
Occidental	151.0	1.5
DuPont	136.0	1.3
Tenneco	89.1	0.9
Amerada Hess	76.5	0.8
City of Long Beach	70.0	0.7
El Paso	67.2	0.7
Union Pacific	59.4	0.6
Superior	57.3	0.6
Santa Fe	44.7	0.4
Mitchell Energy & Devel.	41.9	0.4
Louisiana Land & Expl.	41.4	0.4
Aminoil (R.J. Reynolds)	39.6	0.4
InterNorth	37.5	0.4
Pennzoil	35.1	0.3
Diamond Shamrock	33.4	0.3
Texas Oil & Gas	33.1	0.3
Others (all smaller than the top 30)	3,810.2	37.4
U.S. Total	10,199.0	100.0
Top 4	2,561.3	25.1
8	3,983.0	39.1
15	5,526.6	54.2
20	5,965.4	58.5
30	6,388.8	62.6
HHI (after Texaco/Getty acquisition)		270

TABLE 2

PROVEN U.S. CRUDE OIL, CONDENSATE AND NATURAL GAS LIQUIDS RESERVES, 1982
(Millions of Barrels)

Company	Reserves	Percent of Total
Standard of Ohio	2,855.6	8.1
Exxon	2,836.0	8.1
Atlantic Richfield	2,561.0	7.3
Shell	2,200.0	6.3
Standard of Indiana	1,660.0	4.7
Getty	1,241.0	3.5
Standard of California	1,202.0	3.4
Texaco	1,045.0	3.0
Mobil	906.0	2.6
Gulf	816.0	2.3
Sun	691.0	2.0
Marathon (U.S. Steel)	606.3	1.7
Occidental	583.0	1.7
Union	523.0	1.5
Phillips	492.0	1.4
DuPont	350.0	1.0
Amerada Hess	260.0	0.7
Tenneco	251.7	0.7
Pennzoil	140.0	0.4
Superior	138.7	0.4
Santa Fe	138.3	0.4
Union Pacific	137.6	0.4
El Paso	136.2	0.4
Aminoil (R.J. Reynolds)	120.9	0.3
Mitchell Energy & Devlp.	111.6	0.3
Southland Royalty	81.8	0.2
Texas Oil and Gas	79.3	0.2
Louisiana Land & Expl.	69.0	0.2
Enserch	61.5	0.2
Kerr-McGee	60.1	0.2
Others (all smaller than the top 30)	12,724.4	36.3
U.S. Total	35,079.0	100.0
Top 4	10,452.6	29.8
8	15,600.6	44.5
15	20,217.9	57.6
20	21,358.3	60.9
30	22,354.6	63.7
HHI (after Texaco/Getty acquisition)		329

TABLE 3

DOJ 1982 MERGER GUIDELINES

HHI	ACTION
Post-Merger HHI Below 1000	Unlikely to Challenge
Post-Merger HHI Between 1000 and 1800	
Change in HHI below 100	Unlikely to Challenge
Change in HHI above 100	More likely than not to Challenge
Post-Merger HHI above 1800	
Change in HHI below 50	Unlikely to Challenge
Change in HHI between 50 and 100	More likely to Challenge, depending on other factors
Change in HHI above 100	Likely to Challenge

The numerical standards embodied in the 1982 Justice Department Merger Guidelines ("Guidelines") use the "Herfindahl-Hirschmann" index, often abbreviated as the "HHI" index. In a nutshell, the likelihood of a government challenge to a merger between competitors is based upon the post-merger HHI index and the size of the HHI change caused by the merger. For example, a challenge is unlikely under any facts when the HHI value after the merger is below 1000 "points". At the other extreme, a challenge is likely when the merger increases the HHI index by more than 100 points to above the 1800 level. Table 3 summarizes these standards.

Applying these enforcement guidelines to the market for crude oil, it can be seen that no merger between competing oil companies is likely to be challenged based on its effects in the overall crude oil market. The HHI measured in terms of U.S. production is only about 270 and in terms of U.S. crude oil reserves is approximately 329.[5] All of these values are well below the 1000 HHI level that normally triggers potential antitrust concern with a merger between competitors.

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[5] This discussion assumes the United States as the relevant geographic market. See FTC Report "Mergers in the Petroleum Industry," supra, at 149-54.

B. 1968 Guidelines

A similar enforcement policy was indicated under what are widely viewed as the more stringent enforcement standards of the (now superseded) 1968 Department of Justice Merger Guidelines. The 1968 guidelines for horizontal mergers applied a set of market-share-based numerical standards to determine whether the Department was likely to challenge a given merger between competitors. Which of three "bright-line" market share tests applied to a given merger depended upon whether the market was "highly concentrated" (then defined as one in which the top four firms accounted for 75 percent or more of sales), "less highly concentrated" (the top four firms having a combined share of less than 75 percent), or to be experiencing a "significant trend toward concentration".

In terms of the 1968 Guidelines, the overall crude oil market would clearly not fall into the strictest "highly concentrated" category. The top four firms combined have nowhere near a 75 percent market share. Similarly, it is highly unlikely that, despite the recent increase in oil merger activity, the crude oil market could qualify as one having a significant trend toward increased concentration under the definition of the 1968 Guidelines. Indeed, from 1970 to 1982 concentration in crude oil production decreased slightly.

Thus, the applicable standards would be those of the "less highly concentrated" category. Based upon 1982 production figures, only a merger between two of the top five crude oil producers (i.e., Exxon, Sohio, Arco, Texaco, and Shell) or of the top five holders of crude oil reserves (the same firms) would "ordinarily" have been challenged by the Department of Justice under the 1968 Guidelines. Only in a merger involving two of those five firms would both the acquiring and acquired oil company have crude oil market shares of five percent or more.

To see this, consider an application of the 1968 Guidelines standards (merger between a firm with five percent or more and competitor with five percent or more will ordinarily be challenged) to the recent Texaco/Getty merger. Texaco, with a 3.5 percent market share in crude oil production, acquired Getty, with 2.7 percent of crude production. If crude reserves were used to measure market shares (in place of production) the result is similar. Getty's share of known crude oil reserves was higher than its percentage of production; its merger with Texaco resulted in Texaco, with 3.0 percent of crude reserves, acquiring Getty's 3.5 percent of crude reserves. Under either measure, the five percent/five percent standard is not met.

It is worth noting that the Federal Trade Commission has abandoned strict reliance on concentration in deciding whether to bring merger cases. In 1982, a unanimous Commission, including members appointed by three different Presidents, wrote that "an increase in the threshhold market shares is clearly justified"

and that "consideration of additional market characteristics [beyond market share], entry barriers being the major example, may provide a clearer and more accurate picture of the competitive dynamics."[6]

In any event, under either the more stringent 1968 merger guidelines or the superior 1982 guidelines, the relevant product market that has been cited as most troublesome by some critics of petroleum mergers -- the production of crude oil -- was not sufficiently concentrated in the Texaco/Getty merger to trigger the government's merger enforcement standards.

Of course, in each petroleum merger investigation the Commission will analyze each possible product and geographic market in which the merging firms are competitors -- using the standards of its own Horizontal Merger Statement and the Department of Justice's 1982 Merger Guidelines -- to assess the likely competitive effects of the merger. When it finds competitive overlaps of a magnitude sufficient to endanger competition, the Commission will do what it has done in every petroleum merger it has reviewed: it will take whatever law enforcement action is necessary to prevent injury to competition.

IV. Conclusion

The Commission has developed considerable expertise over the past years in analyzing the competitive impact of mergers in the petroleum industry. In each such merger, it has been able to complete its antitrust review under the Hart-Scott-Rodino procedures and has taken law enforcement action necessary to assure that no unlawful lessening of competition results. The Commission has gone on record as being opposed to any merger moratorium legislation on the ground that such a law is unnecessary to prevent anticompetitive mergers, and would constitute an unwarranted interference with market forces. I believe that position remains sound. Thus, the Committee should be advised that, while there may be other reasons underlying the adoption of any such legislation, such a measure is neither essential for, nor certain to contribute to, the preservation of a competitive oil industry for the benefit of the American consumer.

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6 FTC Statement Concerning Horizontal Mergers, at 3 (June 14, 1982).

Bureau of Competition
FEDERAL TRADE COMMISSION
WASHINGTON, D.C. 20580

JUDICIARY COMMITTEE
1984 JUL -5 PM 3 09
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June 29, 1984

The Honorable Strom Thurmond
Chairman
Committee on the Judiciary
United States Senate
Washington, D.C. 20510

Dear Mr. Chairman:

Thank you for your letter of April 17, 1984, enclosing questions that Senator Kennedy has requested that the FTC answer for the record of the Senate Judiciary hearing of March 15th of this year on oil company mergers. Those questions concern possible divestiture of Gulf Corporation ("Gulf") refining and marketing assets as a consequence of Gulf's acquisition by Standard Oil Company of California ("Socal"). I regret the delay in responding to your letter; we encountered unanticipated delays in preparing the enclosed materials responsive to Senator Kennedy's questions.

As you know, on April 26, 1984, the Commission provisionally accepted for public comment and review a consent agreement with Socal and Gulf containing a consent order to divest and to cease and desist in settlement of a proposed complaint. That complaint alleges that Socal's acquisition of Gulf, as originally proposed, would violate Section 7 of the Clayton Act and Section 5 of the Federal Trade Commission Act. Because the proposed consent order is intended to remedy all of the antitrust problems arising from the acquisition, the Commission did not seek to enjoin the acquisition by a preliminary injunction action in federal court under Section 13(b) of the FTC Act, 15 U.S.C. § 53 (b).

Pursuant to Section 2.34 of its published Rules of Practice and Procedure, the Commission has placed the proposed consent order, the proposed complaint, and an analysis of the proposed consent order on the public record for 60 days, so that interested parties may comment. A copy of the Federal Register Notice containing those documents is enclosed. At the end of the 60-day period, the Commission will review the consent agreement and the comments received and will decide whether it should reject the agreement or make final the agreement's proposed order. If the Commission rejects the agreement, it may: (1) determine that no relief is required; (2) attempt to negotiate with Socal any necessary modifications in the proposed consent order; or (3) take any other action it deems appropriate, including the initiation of litigation to compel Socal to divest certain assets or to seek other relief consistent with Section 7 of the Clayton Act or Section 5 of the Federal Trade Commission Act.

In conjunction with its provisional acceptance of the proposed consent, the Commission has approved an "Agreement To Hold Separate" between Socal and the Commission. This agreement, incorporated as part of the consent order, will maintain the separate identity and individual viability of Gulf's domestic oil and gas assets during the public comment period. The purpose of this agreement is to preserve the likelihood of effective relief should the Commission decide to initiate litigation to compel Socal to divest any assets. Should the consent order be accepted as final, the hold separate agreement will become part of the Commission's divestiture order and will continue in effect until all divestitures have received Commission approval. The hold separate agreement is also contained in the enclosed Federal Register notice.

With regard to Senator Kennedy's first specific question, Paragraph II.B of the proposed consent order specifies Socal's obligations to supply crude oil if necessary to assure the viability of a divested Gulf refinery. That paragraph states:

> Socal shall provide prospective acquirers of the Schedule A Properties [which include a Gulf refinery that Socal must divest] petroleum product exchanges, crude oil supply arrangements, or equity crude oil arrangements if necessary to ensure divestiture of the Properties as ongoing viable enterprises engaged in the same businesses in which the Properties are presently employed.

With regard to Senator Kennedy's second question, a number of terms in the proposed consent order should ensure the viability of the divested entity as an integrated petroleum company. The order requires Socal to sell the Gulf refinery (and associated assets) together with Gulf's entire Southeast wholesale and retail marketing system. This system covers six states and a contiguous portion of a seventh, a region now served by the Gulf refinery to be sold. Thus, Socal must sell a vertically integrated petroleum entity.

The term "viability" encompasses the price, quantity, and credit terms that the divested refinery would be able to offer to customers. In addition to the crude oil assurances set out in II.B of the consent, paragraph II.A of the consent permits the Commission to include in any divestiture any other pipeline, refining, and marketing assets necessary to ensure the divestiture of Gulf's refining and marketing assets as an ongoing viable enterprise.

Based on the purpose of the proposed consent set out in II.D -- "to ensure the continuation of the assets as ongoing, viable enterprises engaged in the same businesses in which the Properties are presently employed and to remedy the lessening of competition resulting from the Acquisition as alleged in the Commission's complaint" -- the Commission may reject any potential buyer who could not manage the assets as a viable ongoing concern. Moreover, the proposed consent contains a powerful incentive for Socal to effectuate a viable divestiture on an expedited basis. Under Paragraph II.C of the proposed consent, Socal would not be permitted to consolidate Gulf's oil and gas assets until the Commission has approved all required divestitures.

Thank you again for your letter. If you have any additional questions or would like to discuss this matter further, do not hesitate to call me (523-3601). Please let me know whenever we may be of service.

Sincerely yours,

Timothy J. Harris

Timothy J. Harris
Director

Enclosure

federal register

Thursday
June 7, 1984

Part VII

Federal Trade Commission

16 CFR Part 13

Socal Inc. and Gulf Corp.; Proposed Consent Agreement With Analysis To Aid Public Comment

FEDERAL TRADE COMMISSION

16 CFR Part 13

[File No. 841-0109]

Socal Inc. and Gulf Corp.; Proposed Consent Agreement With Analysis To Aid Public Comment

AGENCY: Federal Trade Commission.

ACTION: Proposed Consent Agreement.

SUMMARY: The Federal Trade Commission has provisionally accepted a consent agreement with Standard Oil Company of California, "Socal", and Gulf Corporation, "Gulf", in settlement of a complaint alleging violations of section 7 of the Clayton Act and section 5 of the Federal Trade Commission Act. The consent agreement, accepted subject to final Commission approval, would require Socal to sell ("divest") within six months all Gulf assets listed in Schedule A to a Commission-approved buyer(s). Specifically, the proposed consent order would require Socal (among other things) to divest certain of Gulf's petroleum-related assets, including: (a) Gulf's petroleum product wholesale and retail marketing assets in all or part of seven southeastern states; (b) one of Gulf's two refineries on the Gulf Coast; (c) Gulf's interest in the Colonial Pipeline (which transports refined light products to much of the eastern United States); and (d) more than half of Gulf's crude oil pipeline interests in western Texas. The Commission may require Socal to add certain additional assets to any divestiture package. Further, if necessary to achieve effective divestiture, Socal must supply or divest crude oil to the buyer(s) of the divested assets to ensure that the divested entities can be operated as viable, ongoing enterprises, engaged in the same businesses in which the properties are presently employed.

In addition to provisional acceptance of the proposed consent order, the Commission has entered into an "Agreement to Hold Separate" with Socal and Gulf. This agreement will require Socal and Gulf to maintain the separate identity and individual viability of Gulf's oil and gas assets during the public comment period. The consent order extends the Agreement to Hold Separate until Socal has completed all of the required divestitures.

Socal would be prohibited for 10 years from acquiring, without prior Commission approval, any interest in any pipeline transportation, refining, or wholesale marketing assets in Tennessee, Kentucky, the East Coast, the Gulf Coast, the Caribbean, or the Bahamas.

DATE: Comments must be received on or before August 6, 1984.

ADDRESS: Comments should be directed to: FTC/S, Office of the Secretary, Washington, D.C. 20580.

FOR FURTHER INFORMATION CONTACT: FTC/CS-4, Marc G. Schildkraut, Washington, D.C. 20580, (202) 724-1434.

SUPPLEMENTARY INFORMATION: Pursuant to section 6(f) of the Federal Trade Commission Act, 38 Stat. 721, 15 U.S.C. 46 and § 2.34 of the Commission's Rules of Practice (16 CFR 2.34), notice is hereby given that the following consent agreement containing a consent order to cease and desist and an explanation thereof, having been filed with and accepted, subject to final approval by the Commission, has been placed on the public record for a period of sixty (60) days. Public comment is invited. Such comments or views will be considered by the Commission and will be available for inspection and copying at its principal office in accordance with § 4.9(b)(14) of the Commission's Rules of Practice (16 CFR 4.9(b)(14)).

List of Subjects in 16 CFR Part 13

Gasoline, Mergers, Petroleum products, Trade practices.

Before Federal Trade Commission

[File No. 841-0109]

Agreement Containing Consent Order

In the matter of Standard Oil Company of California, a corporation, and Gulf Corporation, a corporation.

The Federal Trade Commission ("the Commission"), having initiated an investigation of the proposed acquisition of shares of Common Stock of Gulf Corporation ("Gulf") by Standard Oil Company of California ("Socal") and Socal and Gulf having been furnished with a copy of a draft complaint that the Bureau of Competition has presented to the Commission for its consideration, and which, if issued by the Commission, would charge Socal and Gulf with violations of the Clayton Act and Federal Trade Commission Act, and it now appearing that Socal and Gulf are willing to enter into an agreement containing an order to divest certain assets and to cease and desist from certain acts:

It is hereby agreed by and between Socal and Gulf, by their duly authorized officers and their attorneys, and counsel for the Commission that:

1. Socal is a corporation organized under the laws of Delaware with its executive offices at 225 Bush Street, San Francisco, California 94101. Gulf is a corporation organized under the laws of Delaware with its executive offices at Gulf Building, Pittsburgh, Pennsylvania 15230.

2. Socal and Gulf admit all jurisdictional facts set forth in the attached draft of complaint.

3. Socal and Gulf waive:

a. Any further procedural steps;

b. The requirement that the Commission's decision contain a statement of findings of fact and conclusions of law;

c. All rights to seek judicial review or otherwise challenge or contest the validity of the order entered pursuant to this agreement; and

d. All rights under the Federal Access to Justice Act.

4. This agreement shall not become a part of the public record unless and until it is accepted by the Commission. If this agreement is accepted by the Commission, it, together with the draft of complaint contemplated thereby, will be placed on the public record for a period of sixty days and information in respect thereto publicly released. The Commission thereafter may either withdraw its acceptance of this agreement and so notify Socal or Gulf, in which event it will take such action as it may consider appropriate, or issue and serve its complaint (in such form as the circumstances may require) and decision, in disposition of the proceeding.

5. This agreement is for settlement purposes only and does not constitute an admission by Socal and Gulf that the law has been violated as alleged in the draft of complaint here attached.

6. This agreement contemplates that, if it is accepted by the Commission, and if such acceptance is not subsequently withdrawn by the Commission pursuant to the provisions of Section 2.34 of the Commission's Rules, the Commission may, without further notice to Socal and Gulf, (1) issue its complaint corresponding in form and substance with the draft of the complaint attached hereto and its decision containing the following order to divest and to cease and desist in disposition of the proceeding, and (2) make information public with respect thereto. When so entered, the order to divest and to cease and desist shall have the same force and effect and may be altered, modified or set aside in the same manner and within the same time provided by statute for other orders. The order shall become final upon service. Delivery by the U.S. Postal Service of the complaint and decision containing the agreed-to order to Socal's and Gulf's addresses as stated in this agreement shall constitute

officers or employees of Socal or Gulf, who may have counsel present, regarding such matters.

VI

It is further ordered that Socal notify the Commission at least thirty days prior to any change in the corporation such as dissolution, assignment or sale resulting in the emergence of a successor corporation, the creation or dissolution of subsidiaries or any other change that may affect compliance obligations arising out of the order.

Schedule A

Assets to be divested as provided above are the following:

1. All of Gulf's marketing assets, including the Gulf brand name and trademark, located in the States of Kentucky, Tennessee, Alabama, Mississippi, Georgia and Florida, and the area of South Carolina served by Gulf's Spartanburg, South Carolina terminal and either the Port Arthur or Alliance refinery, including all associated on-site facilities and dedicated pipelines and terminals. (Socal may elect to divest either refinery, provided that the divestiture of that particular refinery is approved by the Commission).

2. Gulf's stock interest in Colonial pipeline.

3.a. If Socal divests the Port Arthur refinery, then along with the paragraph 1 assets of this Schedule, 51 percent of Gulf's interest in (i) the West Texas Gulf Pipeline Company, (ii) the Mesa Pipeline, and (iii) any other pipeline attached to the West Texas Gulf or Mesa pipelines.

b. If Socal divests the Alliance refinery, then a 51 percent of Gulf's interest in the West Texas Gulf Pipeline Company.

Before Federal Trade Commission

[File No. 841-0109]

Agreement To Hold Separate

In the Matter of Standard Oil Company of California, a corporation, and Gulf Corporation, a corporation.

Agreement dated as of April 20, 1984 (the "Agreement"), by and between Standard Oil Company of California ("Socal"), a corporation organized and existing under the laws of Delaware, whose executive offices are located at 225 Bush Street, San Francisco, California 94104, Gulf Corporation ("Gulf"), a corporation organized and existing under the laws of Delaware, whose executive offices are located at the Gulf Building, Pittsburgh, Pennsylvania 15230, and the Federal Trade Commission ("the Commission"), an independent agency of the United States Government, established under the Federal Trade Commission Act of 1914, 15 U.S.C. section 41, et seq. (collectively, the "Parties").

Premises

Whereas, Socal commenced on March 7, 1984, a tender offer for all of the outstanding shares of Common Stock of Gulf Corporation, a Delaware corporation ("Gulf"), with the intent of effecting a merger of Socal Acquisition Corporation, a Delaware corporation wholly owned by Socal ("Subsidiary"), into Gulf, pursuant to which Gulf would become a wholly owned subsidiary of Socal, all as contemplated and provided for in that certain Merger Agreement entered into among Socal, Subsidiary and Gulf on March 5, 1984 (the "Merger Agreement"); and

Whereas, simultaneously with the execution of the Merger Agreement, on March 5, 1984, Socal and Gulf also entered into a Stock Option Agreement (the "Stock Option Agreement" pursuant to which Gulf granted Socal an option to purchase 30,500,000 authorized but unissued shares of Gulf's Common Stock, constituting approximately 13.6 percent of the shares of Gulf's Common Stock that would be outstanding after such issuance; and

Whereas, the Commission is now investigating the transactions contemplated by the Merger Agreement and the Stock Option Agreement (which transactions are hereinafter referred to as the "Acquisition") to determine if the Acquisition would violate any of the statutes enforced by the Commission; and

Whereas, if the Commission accepts the attached Agreement Containing Consent Order ("Consent Order") the Commission must place it on the public record for a period of at least sixty and may subsequently withdraw such acceptance pursuant to the provisions of § 2.34 of the Commission's Rules; and

Whereas, the Commission is concerned that if an understanding is not reached preserving the status quo ante of Gulf's oil and gas assets and businesses during the period prior to the divestiture of the properties described on Schedule A of the Consent Order ("Schedule A Properties") along with such other assets as may be required under paragraph II of the Consent Order, or the Acquisition is not preliminarily enjoined, divestiture resulting from any proceeding challenging the legality of the Acquisition might not be possible or might be a less than effective remedy; and

Whereas, the Commission is concerned that if the Acquisition is consummated, it will be necessary to preserve the Commission's ability to require the divestiture of properties described in paragraph II of the Consent Order in addition to the Schedule A Properties, and the Commission's rights to seek to restore Gulf as a viable competitor.

Whereas, the purpose of this Agreement and the Consent Order is to preserve Gulf as a viable, integrated petroleum company pending the divestiture of the Schedule A Properties as viable, ongoing enterprises, in order to remedy any anticompetitive effects of the Acquisition and to preserve Gulf as a viable, integrated petroleum company in the event that divestiture is not achieved; and

Whereas, Socal's and Gulf's entering into this Agreement shall in no way be construed as an admission by Socal or Gulf that the Acquisition is illegal; and

Whereas, Socal and Gulf understand that no act or transaction contemplated by this Agreement shall be deemed immune or exempt from the provisions of the antitrust laws or the Federal Trade Commission Act by reason of anything contained in this Agreement.

Now, Therefore, the Parties agree, upon the understanding that the Commission has not yet determined whether the Acquisition will be challenged, and in consideration of the Commission's agreement that, unless the Commission determines to reject the Consent Order, it will not seek further relief from Socal with respect to the Acquisition, except that the Commission may exercise any and all rights to enforce this Agreement and the Consent Order to which it is annexed and made a part thereof, and in the event the required divestitures are not accomplished, to seek divestiture of all Gulf's oil and gas assets and businesses held separate pursuant to this Agreement, as follows:

1. Socal and gulf agree to execute and be bound by the attached Consent Order.

2. Socal agrees that, until (i) three business days after the Commission withdraws its acceptance of the Consent Order pursuant to the provisions of § 2.34 of the Commission's Rules; or (ii) if the Commission within 120 days after publication in the Federal Register of the Consent Order finally accepts such order, until all of the divestitures required by Schedule A of the Consent Order are approved by the Commission, Socal will hold Gulf's oil and gas assets and businesses, as defined in 2(a),

respectively and agree on the following terms and conditions:

a. All Gulf's domestic crude oil and gas assets and operations relating to domestic crude oil and gas exploration and production, and transportation as well as petroleum and petrochemical processing, refining, transportation and marketing activities, and any similar foreign activities to the extent involved in imports into the United States ("oil and gas assets and businesses") shall be operated independently of Socal.

b. Socal shall not exercise direction or control over, or influence directly or indirectly, any of Gulf's oil and gas assets and businesses; provided, however, that Socal may exercise only such direction and control over Gulf as is necessary to assure compliance with this Agreement.

c. Except as required by law and except to the extent that necessary information is exchanged in the course of evaluating the Acquisition, defending litigation, or negotiating agreements to dispose of assets, Socal shall not receive or have access to, or the use of, any "material confidential information" relating to Gulf's oil and gas assets and businesses not in the public domain, except as such information would be available to Socal in the normal course of business if the Acquisition had not taken place. Any such information that is obtained pursuant to this subparagraph shall only be used for the purposes set out in this subparagraph. ("Material confidential information" as used herein means competitively sensitive or proprietary information not independently known to Socal from sources other than Gulf and includes, but is not limited to, customer lists, price lists, marketing methods, geological and geophysical data, patents, technologies, processes, or other trade secrets.)

d. Socal shall not change the composition of the management of Gulf's oil and gas assets and businesses except that the current Gulf directors serving on the "New Board" (as defined in paragraph f) shall have the power to remove employees for cause; Socal shall maintain the viability and marketability of Gulf's oil and gas assets and businesses and shall not sell, transfer, encumber, or otherwise impair their marketability or viability (other than in the normal course of business or pursuant to paragraph h).

e. All material transactions, out of the ordinary course of business and not precluded by paragraph 2(a)-(d), shall be subject to a majority vote of the New Board (as defined in paragraph f).

f. Socal may adopt new articles of incorporation and by-laws (provided that they are not inconsistent with other provisions of this Agreement) and may elect a new Board of Directors of Gulf ("New Board") once it is a majority shareholder of Gulf. Socal may elect any number of directors to the Board; provided, however, that such Board shall consist of at least six current Gulf directors and no more than two Socal directors, officers, employees, or agents. Except as permitted by this agreement, the directors of Gulf who are also Socal directors, officers, employees or agents, shall not receive in their capacity as directors of Gulf material confidential information relating to Gulf's oil and gas assets and businesses and shall not disclose any such information they may receive under this agreement to Socal or use it to obtain any advantage for Socal. Said Directors of Gulf who are also Socal directors, officers, employees, or agents, shall enter a confidentiality agreement prohibiting disclosure of confidential information. Such directors shall participate in matters which come before the New Board only for the limited purpose of considering a capital investment or other transactions exceeding $50,000,000 and carrying out Socal's and Gulf's responsibility to assure that the Schedule A Properties and such other properties as the Commission may elect to add under paragraph II of the Consent Order are maintained in such manner as will permit their divestiture as ongoing, viable assets. Except as permitted by this agreement, such directors shall not participate in any matter, or attempt to influence the votes of the other directors with respect to matters that would involve a conflict of interest if Socal and Gulf were separate independent entities. Meetings of the board during the term of this Agreement shall be stenographically transcribed and the transcripts retained until two years after the termination of this Agreement.

g. The New Board may transfer the properties described in Schedule A of the Consent Order ("Schedule A Properties") into a wholly owned Gulf subsidiary or division.

h. Nothing herein shall prevent the current Gulf Board or the New Board from negotiating or entering into agreements to dispose of Gulf's assets, provided that any such agreements with respect to oil and gas related assets and businesses are conditioned on and not consummated prior to final approval by the Commission.

i. Nothing contained in this Agreement shall be construed to limit the sale of Gulf's nonpetroleum related assets by majority vote of the full current Gulf Board or New Board. Socal shall have the right to borrow all proceeds from any such sale in exchange for an interest bearing note equivalent of the General Motors Acceptance Corporation short term thirty day rate) made payable to Gulf and falling due fourteen days after any denial of final approval of the Consent Order by the Commission.

j. A majority of the New Board may declare a dividend and payment no greater than the amount paid in the same quarter in 1983. Except for such dividend payment, all earnings and profits of Gulf shall be retained separately in Gulf. Socal shall have the right to borrow monies from Gulf upon approval by the majority of the New Board on the same terms and conditions as described in paragraph (i); provided, however, Socal shall not borrow funds if the result would be to impair Gulf's ability to operate its oil and gas assets and businesses at its 1983 levels of expenditure on an annualized basis.

k. Should the Federal Trade Commission seek in any proceeding to compel Socal to divest itself of the shares of Gulf Common Stock it shall acquire, or to compel Socal or Gulf to divest themselves of any oil and gas assets that may be held by either company, or to seek any other injunctive or equitable relief, neither Socal nor Gulf shall raise an objection based upon the expiration of the applicable Hart-Scott-Rodino Antitrust Improvements Act waiting periods or the fact that the Commission has permitted the Gulf Common Stock to be acquired and a formal merger concluded pursuant to the terms of this Agreement. Socal and Gulf also waive all rights to contest the validity of this Agreement.

3. For the purpose of determining or securing compliance with this Agreement, subject to any legally recognized privilege, and upon written request with reasonable notice to Socal or Gulf made to its principal office, Socal and Gulf shall permit any duly authorized representative or representatives of the Commission:

a. Access during the office hours of Socal and Gulf, in the presence of counsel, to inspect and copy all books, ledgers, accounts, correspondence, memoranda and other records and documents in the possession or under the control of Socal or Gulf relating to compliance with this agreement.

b. Upon five days notice to Socal or Gulf and without restraint or interference from them, to interview officers or employees of Socal or Gulf, who may have counsel present, regarding any such matters.

No information or documents obtained by the Commission shall be divulged by any representative of the Commission, except in the case of legal

proceedings to which the Commission is a party, or for the purpose of securing compliance with this Consent Order, or as otherwise required by law.

If, at any time information or documents are furnished by Socal and Gulf and Socal or Gulf identify same as "Confidential," then the Commission shall provide to Socal and Gulf ten days notice or, if ten days is not possible, as many days notice as possible prior to divulging such material in any legal proceeding to which that entity is not a party.

4. This Agreement shall not be binding until approved by the Commission.

John H. Carley,

General Counsel, Federal Trade Commission, Washington, D.C. 20580.

Charles B. Renfrew,

Director and Vice President, Legal, Standard Oil Company of California, 225 Bush Street, San Francisco, California 94104.

Samuel W. Murphy, Jr.,

Senior Vice President and General Counsel, Gulf Corporation.

Before Federal Trade Commission

Complaint

In the matter of Standard Oil Company of California, a corporation, and Gulf Corporation, a corporation.

The Federal Trade Commission, having reason to believe that respondent, Standard Oil Company of California, a corporation subject to the jurisdiction of the Federal Trade Commission, intends to acquire, or has acquired the stock or assets of respondent Gulf Corporation, in violation of section 7 of the Clayton Act, as amended (15 U.S.C. 18), and Section 5 of the Federal Trade Commission Act, as amended (15 U.S.C. 45), and that a proceeding in respect thereof would be in the public interest, hereby issues its complaint, pursuant to section 11 of the Clayton Act (15 U.S.C. 21) and section 5(b) of the Federal Trade Commission Act (15 U.S.C. Section 45(b), stating its charges as follows:

I. Definitions

1. For purposes of this complaint, the following definitions shall apply:

a. "Socal" means Standard Oil Company of California, its predecessors, subsidiaries, divisions, groups, affiliate entities, and each of their past or present director, officers, employees, agents and representatives; and each partnership, joint venture, joint stock company or concession in which Socal is a participant. The words "subsidiary," "affiliate" and "joint venture" refer to any partial (10 percent or more) as well as total ownership or control.

b. "Gulf" means Gulf Corporation, its predecessors, subsidiaries, divisions, groups, affiliate entities, and each of their past or present directors, officers, employees, agents and representatives; and each partnership, joint venture, joint stock company or concession in which Gulf is a participant. The words "subsidiary," "affiliate" and "joint venture" refer to any partial (10 percent or more) as well as total ownership or control.

c. "The acquisition" means the transaction described, in whole or in part, in paragraph 14 of this Complaint.

d. "Gasoline" means motor gasoline as defined in connection with Department of Energy Form EIA–810, Monthly Refinery Report, product codes 132 and 133.

e. "Kerosene jet fuel" means kerosene-type jet aircraft fuel, as defined in connection with Form EIA–810, Monthly Refinery Report, product code 213.

f. "Fuel oil" means the products commonly known as number two fuel oil (home heating, diesel), as defined in connection with Department of Energy Form EIA–810, Monthly Refinery Report, product code 411.

g. "Terminal" means a facility used for recipt, storage, and distribution of gasoline, fuel oil, or kerosene jet fuel, and which receives product directly via pipeline, navigable waterway or from an adjacent refinery.

h. "Refined light products" means gasoline, fuel oil, kerosene jet fuel, and aviation gasoline.

i. "PADD" means Petroleum Administration for Defense District.

II. Respondents

A. Socal. 2. Respondent Socal is a corporation organized and doing business under the laws of the state of Delaware with its executive offices at 225 Bush Street, San Francisco, California 94104.

3. Respondent Socal is a fully integrated petroleum company, engaged in the exploration for and production of crude oil and natural gas, refining, the transportation of crude oil, natural gas and refined products, and the distribution and marketing of refined products and natural gas.

4. In 1982, respondent Socal has revenues of about $34 billion and assets of about $23 billion.

5. In 1982, respondent Socal ranked seventh in the United States in crude oil production, seventh in domestic crude oil reserves, first in refining capacity, and seventh in gasoline sales.

6. Respondent Socal has refineries located at Pascagoula, Mississippi; Perth Amboy, New Jersey; Baltimore, Maryland; El Paso, Texas; Salt Lake City, Utah; Richmond, California; El Segundo, California; Kenai, Alaska; Bakersfield, California; Honolulu, Hawaii; Willbridge, Oregon; and Seattle, Washington, with a combined refining capacity of 1261 thousand barrels per day.

7. At all times relevant herein, respondent Socal has been and is now engaged in commerce as "commerce" is defined section 1 of the Clayton Act, as amended, 15 U.S.C. 12, and is a corporation whose business is in or affecting commerce as "commerce" is defined in section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

B. Gulf. 8. Respondent Gulf is a corporation organized and doing business under the laws of the state of Delaware with its executive offices at Pittsburgh, Pennsylvania.

9. Respondent Gulf is a fully integrated petroleum company, engaged in the exploration for and production of crude oil and natural gas, refining, the transportation of crude oil, natural gas and refined products, and the distribution and marketing of refined products and natural gas.

10. In 1982, respondent Gulf had revenues of about $28 billion and assets of about $20 billion.

11. In 1982, respondent Gulf ranked eight nationally in crude oil production, tenth in United States crude oil reserves, seventh in United States refining capacity, and sixth in United States motor gasoline sales.

12. Respondent Gulf has refineries located at Port Arthur, Texas; Alliance, Louisiana; Philadelphia, Pennsylvania; and Cincinnati, Ohio, with a combined refining capacity of about 829 thousand barrels per day.

13. At all times relevant herein, respondent Gulf has been and is now engaged in commerce as "commerce" is defined in section 1 of the Clayton Act, as amended, 15 U.S.C. 12, and is a corporation whose business is in or affecting commerce as "commerce" is defined in section 4 of the Federal Trade Commission Act, as amended, 15 U.S.C. 44.

III. The Acquisition

14. On or about March 7, 1984, Socal commenced a cash tender offer for up to 100 percent of the outstanding shares of Gulf common stock at a price of $80 per share with the intent of effecting a merger of Socal Acquisition Corporation, a Delaware corporation wholly-owned by Socal, into Gulf, pursuant to which Gulf would become a wholly-owned subsidiary of Socal, all as

contemplated in that certain merger Agreement entered into among Socal, its subsidiary, and Gulf, on March 5, 1984. Gulf's Board of Directors has approved the tender offer and recommended its acceptance by Gulf shareholders. If all the currently outstanding Gulf common shares are tendered to Socal, the total value of the transaction is about $13.2 billion and, if consummated, it would result in the second largest petroleum company and the second largest industrial corporation in the United States in terms of assets.

IV. Trade and Commerce

A. Kerosene Jet Fuel. 15. One relevant line of commerce in which to evaluate the effects of the acquisition is the manufacture and distribution of kerosene jet fuel.

16. One relevant section of the country is PADDs I and III combined (excluding New Mexico and the following counties in the state of Texas: Hansford, Hutchinson, Carson, Armstrong, Briscoe, Floyd, Crosby, Garza, Borden, Howard, Glasscock, Reagan, Crockett, Terrell, and all counties west thereof) and the West Indies and Caribbean Islands.

17. The kerosene jet fuel market described in paragraphs 15 and 16 are concentrated.

18. Conditions of entry into the manufacture of jet fuel in the relevant section of the country are difficult.

19. Socal and Gulf are direct and substantial competitors in the manufacture and sale of jet fuel in the relevant sections of the country. Socal makes kerosene jet fuel at its refinery at Pascagoula, Mississippi. Gulf makes kerosene jet fuel at its refineries at Port Arthur, Texas; Alliance, Louisiana; and Philadelphia, Pennsylvania.

B. Transportation of Refined Light Products. 20. One relevant line of commerce in which to evaluate the effects of the acquisition is the business of transporting refined light petroleum products from refineries into consuming regions. Within this market, petroleum product pipelines represent another relevant line of commerce.

21. One relevant section of the country is the inland Southeast region composed of portions of Mississippi, Alabama, Georgia, Tennessee, South Carolina, North Carolina and of Virginia.

22. Transportation of refined light petroleum products into the inland Southeast is highly concentrated.

23. Conditions of entry into the business of the transporting refined light products by pipeline into the inland Southeast are difficult.

24. Colonial and Plantation are direct competitors in the business of transporting refined light products by pipeline into the inland Southeast.

25. Gulf owns the largest ownership share of Colonial (28.78 percent).

26. Socal owns the second largest ownership share of Plantation (27.13 percent).

27. Because Gulf owns a share of Colonial and Socal owns a share of Plantation, Socal and Gulf are direct and substantial competitors in the business of transporting refined light product by pipeline into the inland Southeast.

C. Marketing of Gasoline and Middle Distillate. 28. Another relevant line of commerce in which to evaluate the effects of the acquisition is the wholesale distribution of gasoline and middle distillate and submarkets thereof.

29. The relevant sections of the country are the areas served by terminal clusters in or near the following cities and areas:

a. Louisville, Kentucky;
b. Lexington, Kentucky;
c. Huntington, West Virginia; Ashland, Kentucky (combined);
d. Evansville, Indiana; Owensboro, Kentucky (combined);
e. Knoxville, Tennessee;
f. Chattanooga, Tennessee;
g. Mobile, Alabama; Biloxi, Gulfport, Pascagoula, Moss Point, Mississippi; Pensacola, Florida (combined);
h. Montgomery, Alabama;
i. Birmingham, Gadsden, Anniston, Tuscaloosa, Alabama (combined);
j. Atlanta, Georgia;
k. Macon, Georgia;
l. Savannah, Georgia;
m. Greenville, Spartanburg, South Carolina (combined);
n. Panama City, Florida;
o. Tallahassee, Florida;
p. Jacksonville, Gainesville, Florida (combined);
q. Tampa, St. Petersburg, Bradenton, Sarasota, Ft. Meyers, Lakeland, Winterhaven, Florida (combined);
r. Daytona Beach, Orlando, Melbourne, Titusville, Cocoa, Florida (combined);
s. Miami, Ft. Lauderdale, West Palm Beach, Florida (combined).

30. The wholesale gasoline and fuel oil markets described in paragraphs 28 and 29 are concentrated.

31. Conditions of entry into the wholesale distribution of gasoline and fuel oil are difficult.

32. Respondents Socal and Gulf are direct and substantial competitors in the wholesale distribution of gasoline and fuel oil in the relevant sections of the country.

D. Transportation of Crude Oil. 33. One relevant line of commerce in which to evaluate the effects of the acquisition is the transportation of crude oil from producing fields to refineries.

34. One relevant section of the country is the West Texas/New Mexico region, composed of "producing districts 8, 8A and 7C" as defined by the Texas Railroad Commission and "New Mexico-East" as defined by the U.S. Department of Energy.

35. Refinery capacity in the West Texas/New Mexico region is substantially below production in the area, with the result that much production in the area is transported over long distances to refineries on the Gulf Coast and in the mid-continent area.

36. The business of transporting crude oil by pipeline out of West Texas/New Mexico is concentrated.

37. Conditions of entry into the business of the transportation of crude oil by pipeline out of the West Texas/New Mexico region are difficult.

38. Socal is the sole owner of a 20 inch diameter pipeline that runs from the West Texas/New Mexico producing area to El Paso, Texas and supplies crude oil to the Socal refinery and the Texaco refinery at El Paso.

39. Gulf is the largest owner of stock in the West Texas Gulf Pipeline Company and therefore controls the West Texas Gulf Pipeline, a 26 inch and 20 inch diameter pipeline that connects the West Texas/New Mexico producing area with both the Gulf Coast and the Mid-Valley Pipeline at Longview, Texas.

40. Respondents Socal and Gulf are direct and substantial competitors in the business of transporting crude oil by pipeline out of the West Texas/New Mexico region.

V. Effects

41. The effect of the acquisition may be substantially to lessen competition or tend to create a monopoly in each of the relevant lines of commerce and relevant sections of the country in violation of section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45, in the following ways, among others:

a. Actual competition between respondents Socal and Gulf in the relevant lines of commerce and relevant sections of the country will be eliminated;

b. Actual competition between competitors generally in the relevant lines of commerce and relevant sections of the country will be lessened;

c. Concentrations in the relevant lines of commerce and relevant sections of the country will be increased, therefore increasing the likelihood of collusion; and

d. Coordination between existing competitors in the relevant lines of commerce and relevant sections of the country will be increased, therefore increasing the likelihood of collusion.

VI. Violation Charged

42. The proposed acquisition of the stock and assets of Gulf by Socal as set forth in paragraph 14 herein, if consummated, would violate section 7 of the Clayton Act, as amended, 15 U.S.C. 18, and section 5 of the Federal Trade Commission Act, as amended, 15 U.S.C. 45.

Wherefore, the premises considered, the Federal Trade Commission on this day of , A.D. 1984, issues its complaint against respondents Standard Oil Company of California and Gulf Corporation.

Analysis of Proposed Consent Order To Aid Public Comment

The Federal Trade Commission has provisionally accepted an agreement containing a proposed consent order with Standard Oil Company of California ("Socal") and Gulf Corporation ("Gulf").

On April 26, 1984, the Commission entered into a provisional agreement, also containing the proposed consent order, with Socal and Gulf in settlement of a proposed complaint. The proposed complaint states that the Commission has reason to believe that consummation of Socal's acquisition of Gulf ("Acquisition") would violate section 7 of the Clayton Act and section 5 of the Federal Trade Commission Act. The proposed complaint specifically alleges that the Acquisition may substantially lessen competition in several markets: (1) The manufacture of kerosene jet fuel (used by commercial airlines utilizing jet or turboprop aircraft) in the East Coast and Gulf Coast portions of the United States; (2) the wholesale distribution of gasoline and middle distillates (home heating oil and diesel fuel) in a number of cities and areas in the southeastern United States; (3) the transportation of refined light products (distillate fuel oil, aviation gasoline, gasoline, jet fuel, and kerosene) into the southeastern United States; and (4) the transportation of crude oil out of western Texas and eastern New Mexico.

To remedy these alleged anticompetitive results of the Acquisition, the agreement's proposed consent order would (among other things) require Socal to sell ("divest") certain Gulf's petroleum-related assets, including: (a) Gulf's petroleum product wholesale and retail marketing assets in all or part of seven southeastern states; (b) one of Gulf's two refineries on the Gulf Coast; (c) Gulf's interest in the Colonial Pipeline (which transports refined light products to much of the eastern United States); and (d) more than half of Gulf's crude oil pipeline interests in western Texas. As described in greater detail below, the Commission may require Socal to add certain additional assets to any divestiture package. Further, if necessary to achieve effective divestiture, Socal must supply or divest crude oil to buyers of the divested assets to ensure that the divested entities can be operated as viable, ongoing enterprises, engaged in the same businesses in which the properties are presently employed.

The Commission has placed the proposed complaint and the provisionally accepted consent order on the public record for sixty (60) days so that interested parties may comment on it. Comments received during this period will become part of the public record, unless commentors request confidential treatment. *Commentors desiring confidential treatment must do so by printing "Confidential Treatment Requested" across the top of the first page of their comments.* After the end of the sixty day comment period, the Commission will review the proposed complaint and consent order and the comments received thereon, and will decide whether it should withdraw from the consent agreement or make final the agreement's proposed consent order.

If the Commission withdraws from the agreement, it may: (1) Determine that no relief is required; (2) attempt to negotiate with Socal and Gulf any necessary modifications in the proposed consent order; or (3) initiate litigation to compel Socal to divest certain assets or seek any other injunctive or equitable relief consistent with section 7 of the Clayton Act or section 5 of the Federal Trade Commission Act.

In addition to provisional acceptance of the proposed consent order, the Commission has entered into an "Agreement to Hold Separate" with Socal and Gulf. This agreement will maintain the separate identity and individual viability of Gulf's domestic oil and gas assets during the public comment period. The proposed consent order expressly makes the Agreement to Hold Separate a part of the consent order. The consent order extends the Agreement to Hold Separate until Socal has completed the required divestitures.

If, at the end of the comment period, the Commission believes further enforcement action is warranted and withdraws from the proposed consent agreement, the Commission may seek any relief it deems appropriate, including a federal court order under section 13(b) of the Federal Trade Commission Act. In such a court action, the Commission may request (among other things) an extension of the "Hold Separate" provisions in order to prevent any commingling of Gulf's petroleum operations or assets with Socal's until a final adjudication on the merits of any administrative action the Commission may initiate.

The purpose of this analysis is to facilitate public comment on the proposed consent order. It is not intended to constitute an official interpretation of the proposed complaint, consent order, or Agreement to Hold Separate, or to modify in any way their terms. To further assist commentors, the Commission has also placed on the public record copies of a report summarizing the results of its recent in-depth study of mergers in the petroleum industry.[1] That report discusses many of the competitive issues raised by the Acquisition.

The Consent Order

Paragraphs I and II. The introductory paragraph of the proposed consent order defines the terms used in the order.[2] Of particular importance, "Schedule A Properties" are defined to include the assets and businesses that are listed in the Schedule A appendix to the proposed consent order.

Paragraph II of the proposed consent order requires Socal to divest all of the Schedule A Properties, and prescribes some of the terms and conditions for selling the Schedule A Properties. The Schedule A Properties are: (1) Gulf's wholesale and retail marketing assets (including the Gulf trade name) in Kentucky, Tennessee, Alabama, Mississippi, Georgia, Florida, and the Spartanburg area of South Carolina, as well as one of Gulf's two Gulf Coast refineries, located at Port Arthur, Texas and Belle Chase (Alliance), Louisiana;[3] (2) Gulf's interest in the Colonial Pipeline; and (3) 81 percent of Gulf's interest in the West Texas Gulf Pipeline Company (as well as 81 percent of Gulf's interest in all the pipelines

[1] Report of the Federal Trade Commission, Mergers in the Petroleum Industry (1984) (hereinafter "Mergers Study").

[2] The proposed complaint also contains several definitions of standard industry terms.

[3] Socal has the option of divesting either one of these two Gulf refineries.

connected to the West Texas Gulf Pipeline if Socal should divest the Port Arthur refinery).

Subparagraph A of the proposed consent order would require Socal to divest the Schedule A Properties within six [6] months from the date the consent order is given final acceptance by the Commission. The Commission may also require Socal to divest additional oil and gas refining, marketing, transportation, and petrochemical processing assets to ensure that the purchaser of divested properties can operate them as ongoing, viable enterprises engaged in the same businesses in which they are presently used.

Subparagraph B would require Socal to provide prospective buyers with product exchanges or crude oil supply arrangements, or to divest crude oil properties, if necessary to ensure that the properties are divested as ongoing, viable enterprises engaged in the same businesses in which they are presently used.

Subparagraph C makes the Agreement of Hold Separate part of the proposed consent order. Subparagraph C would require Socal to maintain Gulf's oil and gas assets as an independent entity, and would prohibit Socal from exercising control over or consolidating the Gulf operations and properties into Socal until Socal has divested the Schedule A Properties. Subparagraph C extends the duration of the provisions of Paragraph 2 of the Agreement to Hold Separate.

Subparagraph D would require Socal to seek and obtain prior Commission approval of any proposed divestiture required by the consent order. The public at that time would have an opportunity to comment on such divestiture proposals. Finally, Subparagraph E would require Socal and Gulf to maintain the viability and marketability of the assets to be divested, and would prohibit the destruction or impairment of any of those assets.

Paragraphs III and V. Paragraphs III an V of the proposed consent order would permit access by Commission representatives to records and documents of Socal and Gulf to assure compliance with the proposed order.

Paragraph IV. Paragraph IV of the proposed consent order would require prior Commission approval for ten years of any acquisition by Socal of any pipeline transportation, refining, or wholesale marketing assets in Tennessee, Kentucky, the East Coast, the Gulf Coast, the Caribbean, or the Bahamas.

Paragraph VI. Paragraph VI of the proposed consent order would require Socal and Gulf to notify the Commission of any change in corporate structure that may affect their compliance with the order.

Analysis of Potential Competitive Problems.

The divestitures in the proposed consent order (summarized above) are designed to remedy a number of potential competitive problems discussed below.

A. Kerosene Jet Fuel ("Kerojet"). Under Schedule A(1) of the proposed consent order, Socal would have to divest one of Gulf's two Gulf Coast refineries. As alleged in Paragraph IV. A of the proposed complaint, Socal and Gulf are direct and substantial competitors in the manufacture and sale of kerosene jet fuel or "Kerojet" in the Gulf Coast and East Coast. Socal supplies jet fuel in this region from its refineries in Pascagoula, Mississippi and the Bahamas. Gulf supplies the affected region from its refineries at Port Arthur, Texas; Alliance, Louisiana; and Philadelphia, Pennsylvania.

Kerojet is the fuel used by all commercial jet and turboprop aircraft. Kerojet must meet stringent performance and quality specifications. Commercial airlines have no practical substitutes for kerojet.

One important question in measuring the competitive impact of the Acquisition in this kerojet market is whether smaller manufacturers of kerojet may be able to increase supply in response to (and thereby frustrate) any increase in price by large kerojet manufacturers that resulted from the Acquisition. Refiners may have some flexibility to reduce the production of other petroleum products in favor of increased production of kerojet. In practice, however, the types of crude oil inputs used in a particular refinery—the "crude oil slate"—as well as the refinery design may limit this flexibility. Technical and economic constraints that may limit this flexibility include: (1) The fraction from a given type of crude oil that is suitable for the production of kerojet; (2) the difficulty in switching crude oil slates to increase the fraction suitable for the production of kerojet; (3) the need for additional processing facilities to manufacture kerojet; (4) the substantial economic cost penalty of foregoing the alternative use of the fraction suitable for kerojet, such as heating oil.

Because there may be such limits on refiners' flexibility and because commercial airlines have no alternative to kerojet, refiners manufacturing kerojet may be able to raise prices above competitive levels if concentration is high enough in any region of the country that forms a separate economic market.

One such region of the country appears to consist of Petroleum Administration for Defense Districts ("PADDs") I and III. This roughly corresponds to an area including states along the eastern seaboard (PADD I) and the states along the Gulf Coast (PADD III). (PADD III excludes western Texas and New Mexico.) PADDs I and III are connected by product pipelines that transport kerojet and other refined light products (such as gasoline and heating oil) from the Gulf Coast to East Coast and Southeast markets. Most kerojet consumed in PADDs I and III is produced in that region. However, imports do account for about 6 percent of kerojet consumed in that area. Most of these imports originate in the Bahamas and Caribbean Islands.

For PADDs I and III alone (including imports), Socal has an 8.8 percent share of the kerojet market and Gulf has 11.1 percent.[4] The post-acquisition Herfindahl-Hirschman Index ["HHI"][5] for this market would be in excess of 1300 with an increase of approximately 200 points.[6] Including all Caribbean

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[4] Socal and Gulf data submitted in response to the Commission's Request for Additional Information under the Hart-Scott-Rodino Act of 1976 [hereinafter "Response to Commission Request"].

This and additional citations to Socal and Gulf data refer to confidential materials submitted to the Commission for the Commission's competitive review of the Acquisition. Socal and Gulf have waived confidential treatment for the limited purpose of permitting the Commission to cite relevant Socal and Gulf information and data in this analysis.

[5] The Commission has found the HHI to be preferable to four and eight firm concentration ratios for analyzing market structure. One advantage of the index over traditional four-firm concentration ratios is that HHIs "reflect both the distribution of the market shares of the top four firms and the composition of the market outside the top four firms." Grand Union, 3 Trade Reg. Rep. (CCH) ¶ 22481, at 22818.19 (June 16, 1982) [hereinafter "DOJ Merger Guidelines"].

[6] The HHI is calculated by summing the squares of the individual market shares of each firm. DOJ Merger Guidelines, *supra*, at ¶ 22818.10. To place in context the HHI estimates used in this Analysis, it is helpful to note that the Department of Justice has indicated that it is unlikely to challenge an acquisition where the post-acquisition HHI is below 1000. The Department is likely to challenge an acquisition if the acquisition increases the HHI more than 100 points and the post-acquisition increases the HHI more than 100 points and the post-acquisition HHI is between 1000 and 1800. The Department is likely to challenge acquisitions that increase the HHI more than 50 points if the post-acquisition HHI is above 1800. *Id.* at ¶ 22818.101.

"Department of Energy, Form EIA-410 "Refinery Reports"; Department of Energy, Energy Data Reports, "Supply Disposition, and Stocks of All Oils by Petroleum Administration for Defense Districts and Imports Into the United States, By Country," 1983.

Continued

kerojet production would not significantly alter the HHI because the major refiners in the Bahamas and the Caribbean—including Socal—are also major manufacturers of kerojet in PADDs I and III.

The Commission gives considerable weight to the DOJ Merger Guidelines in its evaluation of horizontal mergers and acquisitions. *See* "Statement of Federal Trade Commission Concerning Horizontal Mergers," Trade Reg. Rep. No. 348 (CCH)-(Jun. 14, 1982).

There are a number of additional market factors that may affect the ability of refiners to raise kerojet prices above PADD III excludes West Texas and New Mexico.

There are a number of additional market factors that may affect the ability of refiners to raise kerojet prices above competitive levels after the Acquisition.[7] In balancing these factors, the Commission determined that the merger presented an unacceptable risk that kerojet producers' ability to collude would be enhanced by the Acquisition as originally proposed. To remedy any such competitive problems created by the Acquisition, the proposed consent order would require Socal to divest one of Gulf's two Gulf Coast refineries. Gulf's Port Arthur, Texas, refinery is a large producer of kerojet. Gulf's Alliance, Louisiana refinery, also produces kerojet and some potential buyers may find it a more attractive component of a divestiture package. Granting Socal the option of selling either refinery, therefore, should facilitate compliance with the proposed consent order and help insure the continuation of the divested assets as a viable refining and marketing business.

B. Transportation of Refined Light Products. The Colonial Pipeline ("Colonial") is the largest refined light product pipeline serving the Southeast, with a capacity of about 2.1 million barrels per day. The mainline of Colonial extends from Houston, Texas to Linden, New Jersey (near New York Harbor). Colonial Pipeline is a joint stock company owned by ten oil companies. Gulf owns the largest share.

The only other product pipeline serving the Southeast is the Plantation Pipeline ("Plantation"). Plantation has a capacity of 558,000 barrels per day and extends from Baton Rouge, Louisiana to Washington, D.C. Plantation is also a joint stock company owned by three oil companies. Socal owns the second largest share of Plantation.

Both Colonial and Plantation are vertically integrated through their owners, which all operate refineries.

Because much of the inland Southeast has negligible local refining capacity, and because moving waterborne refined products inland is not cost-effective, this area is dependent on Colonial and Plantation for products such as gasoline and heating oil. Colonial and Plantation directly compete to transport such products to much of the Southeast. The Acquisition would leave Socal as a major owner of the only two major pipelines of this type in the Southeast.

Tariffs (shipping rates) on these pipelines may have been constrained in the past by a combination of federal regulation and by competition. However, a great deal of uncertainty now exists concerning the degree of constraint on oil pipeline tariffs that federal regulation will provide in the future. The Federal Energy Regulatory Commission ("FERC") in its *Williams Pipeline Co.* decision [8] suggested that greater reliance should be placed on competition in tariff setting. Although a Federal Court of Appeals has recently remanded the *Williams* case to FERC,[9] it is unclear at this point how FERC will resolve the regulatory issues on remand.

There has always been an element of tariff competition between Colonial and Plantation. As a Plantation study has commented:

> The level of Colonial's tariffs has generally exerted a downward pressure on Plantation's since the competing system began operating and it will likely do so again in the future.[10]

The two pipelines also compete on the basis of non-tariff factors. For instance, the minimum size per shipment on Plantation is smaller, and Plantation offers special services for the small shipper. Colonial also competes on the basis of services and believes that "shippers may be willing to pay a slightly higher cost to transport products on the Colonial system in preference to the Plantation system because Colonial offers service that better meets their needs."[11]

A third area of competition is for new pipeline connections, which can be more profitable if other pipelines are unlikely to build a lateral line to the same area. Only Plantation, for example, serves the Charlotte, North Carolina, Airport, having constructed a lateral line in 1962. Perhaps because it is the sole line to the airport, Plantation's tariff to that airport from Baton Rouge is 73.66 cents per barrel, a charge of 16 cents per barrel more than its tariff to the city of Charlotte, where Plantation competes with Colonial.[12]

If Socal were to become a major owner of both pipelines, competition between Plantation and Colonial could be unacceptably reduced in violation of section 7 of the Clayton Act and section 5 of the Federal Trade Commission Act, as set forth in Paragraph IV.B of the proposed complaint. To remedy such a violation of law, the proposed consent order would require Socal to divest Gulf's ownership interest in Colonial, as specified in Schedule A(2) of the proposed consent order.

C. Marketing of Gasoline and Middle Distillates. Paragraph IV.C of the Commission's proposed complaint alleges that the Acquisition may tend to lessen competition in the wholesale distribution of gasoline and middle distillates in numerous areas in the Southeast United States. To remedy this concern, Schedule A(1) of the proposed consent order would require Socal to divest Gulf's wholesale and retail marketing assets in a number of southeastern states.

"Wholesale distribution" as used in the proposed complaint means sales from petroleum product "terminals," rather than bulk cargo sales at the refinery or retail sales. These terminals store petroleum products received from pipelines or waterborne vessels and dispense the products into tank trucks for further distribution. The wholesale market consists of an identifiable set of services including the storing, transporting, and dispensing of petroleum products from these terminals.

The relevant geographic markets for wholesale marketing appear to depend on the location of terminals and the distance that gasoline or middle distillates may be shipped economically from these terminals. Terminals tend to cluster in or near urban centers. The areas served by each of these "clusters" are generally smaller than a state but larger than a city. One cluster of terminals is often not in competition

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[7] Figures include foreign imports. Because of incomplete data on the source of imports from the Bahamas and the Netherlands Antilles, an end user allocation was made among the refiners operating in those countries. As noted above, PADD III excludes West Texas and New Mexico.

[8] For instance, substantial new entry into kerojet refining is unlikely because demand for kerojet is relatively "inelastic" (*i.e.*, insensitive to price changes) and the product is homogeneous as it is produced to rigid specifications.

[9] Dkt. No. CR-79-1-000, *et al.*, 23 F.E.R.C. ¶ 61,169 (Nov. 1983).

[10] No. 82-1012, slip op., at 7 (Dec. 9, 1983) 52 U.S.L.W. 2040 (Apr. 3, 1984).

[11] Response to Commission Request.

[12] Response to Commission Request.

[13] Plantation Pipeline Co., FERC tariff 37, effective Dec. 8, 1982.

with other terminal clusters because the cost of trucking product from one cluster to another may be prohibitive. For this reason, Socal and Gulf each deliver on average 75 percent of their product in the Southeast by tank truck within areas less than 50 miles of such terminal clusters.[14]

The Commission has identified a number of potential terminal cluster markets where concentration would increase significantly as a result of the Acquisition, using terminal capacity for gasoline and middle distillate in various terminal cluster areas as the basis for measuring concentration. Based on data submitted to the Commission by the parties, Socal's and Gulf's estimated shares of terminal capacity and post-acquisition HHIs for selected Southeast terminal groups are set forth in Table I:[15]

TABLE I.—SOUTHEAST WHOLESALE TERMINAL CONCENTRATION MEASURES

Terminal location	Socal share [1]	Gulf share [1]	HHI change	Post-acquisition HHI
Louisville, KY	28.4	7.2	396	1669
Paducah, KY	37.5	24.5	1362	3889
Ashland, KY	8.0	13.5	242	3758
Knoxville, TN	9.0	12.9	90	1169
Chattanooga, TN	3.0	14.3	60	1170
Meridian, MS	13.4	12.7	340	1870
Collins, MS	12.0	17.5	407	1745
Mobile, AL	47.1	2.8	264	2918
Birmingham, AL	13.5	8.8	238	2949
Montgomery, AL	12.0	8.8	1058	1119
Albany, GA	12.0	22.4	573	2911
Athens, GA	19.4	22.5	873	2917
Macon, GA	22.7	45.2	2052	2917
Spartanburg, SC	42.8	37.2	4772	5943
Miami, FL	8.5	34.1	580	2897
Jacksonville, FL	8.5	8.5	145	1158
Tampa, FL	15.3	16.2	248	1689
	14.4	18.8	324	1919

[1] In percent.

A number of studies of wholesale gasoline marketing suggest a positive relationship between prices and concentration.[16] To remedy the possibility of a greater likelihood of collusively or monopolistically determined prices as a result of any increase in concentration caused by the Acquisition, Schedule (A)(1) of the proposed consent order requires divestiture of Gulf's wholesale and retail marketing assets— including terminals, bulk plants, warehouses, package plants, tank trucks, service stations, product inventories, storage tanks, and Gulf brand names and trademarks—in Kentucky, Tennessee, Alabama, Mississippi, Georgia, Florida, and the Spartanburg area of South Carolina.

[14] Response to Commission Request.
[15] Response to Commission Request.
[16] *See Morger Study*, supra, n. 1, at 220, and studies cited therein. The Commission concluded that the "evidence may indicate the presence of market power in concentrated markets, but the interpretation of such evidence is fraught with difficulties." *Id.*

Gulf's retail marketing assets in this region would be required to be sold to the buyer of the wholesale marketing assets to ensure successful divestiture of a viable marketing entity. The proposed consent order also contemplates that these wholesale and retail marketing assets will be sold in a package with either Gulf's Port Arthur or its Alliance refinery. In the proposed consent order, the Commission reserves the right to include either refinery as well as any additional pipeline, refining, or marketing assets, to ensure that properties are divested as ongoing, viable enterprises, engaged in the same businesses in which they were used prior to the Acquisition. Further, as noted above, Socal is required to provide prospective buyers with product exchanges or crude oil supply arrangements, or to divest crude oil properties, if necessary to ensure that the properties are divested as ongoing, viable enterprises engaged in the same businesses in which they are presently used.

D. Transportation of Crude Oil. Schedule A(3) of the proposed consent order would require the divestiture of 51 percent of Gulf's interests in certain crude oil pipelines in western Texas. These proposed divestitures are designed to remedy the antitrust concerns set forth in Paragraph IV.D of the proposed complaint. That paragraph alleges that Socal's and Gulf's combined ownership of these pipelines would lessen competition, in violation of section 7 of the Clayton Act and section 5 of the Federal Trade Commission Act.

Both Socal and Gulf own trunk pipelines that transport crude oil out of the West Texas and eastern New Mexico ("West Texas") area to various refining centers. Gulf owns 87 percent of one of the several major pipelines that transports crude oil out of the area, the West Texas Gulf Pipeline. Socal owns 100 percent of another major pipeline that runs from West Texas crude oil fields to El Paso.

Most of the pipelines in the West Texas area are physically interconnected so that crude oil produced in the area can reach their ultimate market by multiple routes. As a result, crude oil trunk pipelines in that geographic area are competitors for transporting the crude oil produced in the West Texas region. Because other modes of transportation are too costly to be a significant competitive threat to these pipelines, it is possible that a coordinated tariff increase by the pipelines' owners could successfully be imposed on West Texas crude producers. These trunk pipelines are in large part owned by refiners who have alternative sources of crude oil. Other firms that are solely crude oil producers and that ship their crude out of West Texas fields on these pipelines may have no alternative but to lower the wellhead price of their West Texas crude oil if it is to remain price competitive with other crudes at the eventual location of sale. This lowered wellhead price could possibly discourage investment either in new sources of West Texas crude oil, or in enhancing recovery from existing wells.

As a result of the Acquisition, the HHI in this transportation market would increase almost 140 points to nearly the 1300 level.[17] The combined Socal-Gulf share would exceed 22 percent.[18]

These figures may, however, understate the anticipated impact on competition, because smaller pipelines in the West Texas market may not be able to increase their throughput substantially enough to displace the larger trunk pipelines if the latter raised tariffs following the Acquisition. At greater throughput levels, the cost of the small pipelines would rise steeply in comparison to the declining costs of the large pipelines. As pipeline diameter increases in size, a more-than-proportional volume of crude oil may be sent through the pipeline, causing costs to decline significantly at higher throughput levels. The larger pipelines may to some extent, therefore, be effectively insulated from offsetting competition from smaller pipelines. Assuming the absence of this competitive "fringe," the post-acquisition HHI would approach 1700 with a change of more than 230 point.[19]

For the reasons described above in discussing the Colonial and Plantation product pipelines, FERC regulation may not act as an effective constraint against supracompetitive tariff increases. Tariff revenues, however, are not the pipeline's only incentive to behave in an anticompetitive manner. This is because Gulf and Socal are fully backward integrated into crude oil production, and forward integrated into refining and marketing. By raising tariffs and lowering crude oil prices, integrated oil firms can reduce their Windfall Profit Tax[20] liabilities, by transferring profits

[17] Response to Commission Request.
[18] Response to Commission Request.
[19] *Id.*
[20] 26 U.S.C. § 4986–4992. The Act imposes a tax on domestic crude oil production (with certain exceptions). The tax is imposed on the holder of the economic interest when the crude oil is removed from the ground. The Commission discussed oil company incentives to maintain below market crude oil prices in its recent notice for public

Comment

from their production subsidiaries to their lower-taxed pipeline and refinery subsidiaries. For non-integrated, independent producers who cannot make such transfers, however, lowering crude oil prices would result in a loss of income that may retard or delay investments in crude oil production.

The proposed consent order would remedy the anticompetitive consequences of the acquisition by requiring divestiture of certain of Gulf's West Texas pipeline interests, depending upon which refinery is actually divested. Gulf's Port Arthur refinery is connected to the West Texas Gulf Pipeline, which is connected through the Mesa Pipeline to additional pipelines that gather crude oil in West Texas. If Socal should divest Port Arthur, 51 percent of Gulf's share of all the above West Texas pipelines must be divested. The new buyer would, thus, be able to rely on Gulf's entire West Texas system to supply crude oil to the Port Arthur refinery. However, if Socal should divest Gulf's alliance refinery in Louisiana, only 51 percent of Gulf's share of the West Texas Gulf Pipeline need be divested: Socal's ability to retain the other Gulf pipeline interests will avoid any disruption of crude oil supplies for the Port Arthur refinery.

Comments Requested

The Commission is interested in receiving public comments on all competition-related issues concerning the Commission's proposed disposition of this matter. Is the antitrust analysis—including the alleged facts and premises underlying this analysis—valid? Are there any antitrust violations other than those identified in the proposed complaint and this analysis that should be addressed? Is the proposed relief appropriate? Are any aspects of the relief too narrow or too broad? Are the competitive problems discussed in this analysis serious enough to justify the proposed remedies?

With regard to specific provisions of the proposed consent order, is it appropriate to require divestiture of Gulf's refining and marketing assets listed in Schedule A(1) as a package? Are there any additional assets that should be included in the package to ensure the divestiture of the properties as ongoing, viable enterprises engaged in refining and marketing, as contemplated by Paragraph II.A of the proposed consent order? Are there any assets that may be excluded from the package without jeopardizing the viability of the divested properties?

If the Commission finally accepts the proposed consent order in its present form or after modification, the Commission will decide then whether to approve any proposed divestiture of the Schedule A Properties following a review of written comments concerning the proposed divestiture submitted during a separate, 30-day public comment period. What criteria should the Commission use to judge the viability of any proposed divestiture and to determine whether additional pipeline, refining, or marketing assets should be added to the proposed divestiture? Paragraph II.B of the proposed consent order requires Socal to provide product exchanges, crude oil supply arrangements, or equity crude oil arrangements if necessary to ensure a viable divestiture. Is this an appropriate provision for the proposed consent order? What criteria should the Commission use to determine whether the product and crude oil arrangements offered by Socal are sufficient?

Is it appropriate to permit divestiture of Gulf's interest in the Colonial Pipeline Company to a third party, or should it be divested in a package with the Schedule A(1) Properties (consisting of Gulf's Southeast marketing assets and one of the two designated Gulf refineries)? Is there any reason to prohibit present owners of the Colonial Pipeline Company from buying Gulf's shares of the line?

Is it appropriate to divest Gulf's share of all Gulf's West Texas Pipeline interests in a package with the Port Arthur refinery? Is is appropriate to require a divestiture of only an interest in the West Texas Gulf Pipeline Company if Socal divests the Alliance refinery?

The proposed consent order requires Socal to hold Gulf's oil and gas assets separate until Socal has accomplished all divestitures required by the proposed consent order. Is this an appropriate method of ensuring that the divestitures are accomplished quickly and in a manner that will preserve competition and permit the affected assets to remain ongoing, viable operations?

Does maintaining effective competition at the refined product wholesale level in the Southeast require Socal to divest all terminals set out in Schedule A(1)? Would an economically viable refinery, distribution, and marketing divestiture require selling this complement of terminals or some other set?

Are there any efficiencies in refining, marketing, or distribution that would result from this Acquisition that would be lost or undone by the proposed divestitures? Would alternative divestitures retain these efficiencies while eliminating any anticompetitive consequences that may result from the Acquisition?

Emily H. Rock,
Secretary.

Dissenting Statement of Commissioner Pertschuk Concerning Socal-Gulf Acquisition, File No. 841-0180, April 25, 1984

I find the decision on this consent agreement to be a far closer question that the *Texaco-Getty* consent agreement or the failure of the Commission to pursue an adequate remedy in the *Mobil-Marathon* case, primarily because the staff has negotiated an agreement which gives some hope that the divested Gulf properties will emerge in an economically viable and competitive posture. For this, credit must be given to the skill and determination of key staff members as well as to the healthy expressions of concerns about past Commission actions by those outside the Commission. Yet I find myself compelled to vote against the agreement and in favor of seeking to enjoin the merger for a number of reasons.

First, it has become increasingly obvious that there are major weaknesses in our procedures for addressing the antitrust problems of huge mergers in a limited period of time and for negotiating massive and compex divestitures. Under the terms of the Hart-Scott-Rodino Act, we have as little as ten days before the Commission must decide whether to challenge a merger after requested information is received from the merging companies. In this case, the largest merger in history, the staff analysis of the consent agreement—the principal document describing the consent agreement and its rationale—was provided to the Commission at about 2:00 P.M. yesterday. Bureau of Economic analyses on key points arrived at 6:00 P.M., and the Bureau Director's memo was furnished at 8:30 P.M. These memos deal with exceedingly complex issues of restructuring Gulf assets and attempting to solve major horizontal overlaps in a series of markets. I do not believe that a responsible evaluation of these issues can be done, including resolving the competing claims of various staff and interested private groups, in the few hours available.

Second, although the consent agreement represents a major improvement over our approach in

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comment concerning Texaco Inc.'s proposed acquisition of Getty Oil Co., 49 FR 9439, 9441-42 (Mar. 7, 1984).

Texaco-Getty, I am still concerned that the divestitures we have in mind risk the selling off and eventual demise of assets which have up till now been viable. A major advantage of this agreement is that it provides for holding Gulf separate until the divestitures are approved and, more importantly, for providing the Commission authority to order *additional* divestitures, including crude oil, to insure the divested assets are continued as "ongoing, viable enterprises." This provision, as well as the staff analysis, recognize the crucial importance of access to crude oil in maintaining viability for refiners and marketers. It is a principle we could have put to better use in the *Texaco-Getty* and *Mobil-Marathon* matters.

However, this hold separate agreement is not the ordinary hold separate procedure employed to preserve the Commission's opportunity to enjoin a merger entirely after a period of investigation or litigation. This hold separate provision is a lever to encourage Socal to divest properties as well as a way of facilitating sale of assets in viable "packages," but it is not a guarantee to the Commission that it can conclude later that the only way the assets can be viable is that the merger itself be rescinded.

The staff candidly admits that "despite the strong guarantees in the consent a refinery-marketing divestiture is not without risks." These risks arise because of the importance of regular access to crude and refined products as well as the powerful incentive Socal has to sell off or close down the least desirable properties it acquires from Gulf. In order to insure that the divested properties remain viable, the Commission will have to oversee complex negotiations between Socal and potential buyers, to make predictions about what the buyers intend to do with purchased assets, and to determine what additional assets, particularly crude supply contracts, are necessary for "viability." As far as I know, the Commission has never assumed responsibility for overseeing such a major restructuring of assets, and it remains to be seen how effective and vigorous it will be in carrying out this difficult job over the coming months.

At the very least, we can expect temporary supply contracts of one sort or another to be negotiated as a part of these sales. Are Socal temporary supply agreements sufficient to get a refinery or marketing assets permanently over some survival threshold, or will they be temporary lifelines only? Further, will such supply contracts in reality be agreed to by potential buyers because they are able to get crude oil at a bargain price, not because they actually intend to operate assets for the long term? Moreover, if this complex divestiture plan begins to fall apart some months from now, what can the Commissioner's options? As I interpret the agreement, we do have a fair amount of discretion in requiring Socal to put additional assets in the divestiture package, but we do *not* have the discretion to throw up our hands and say the only solution is preserving an independent Gulf. By accepting this agreement we are committed to a course in which most of Gulf is absorbed by Socal and some of its least desirable assets are parceled out. There will be no turning back from the basic decision.

I realize that there are limits to how certain we can be about the success of divestitures, but I do not believe the law requires us to take any significant risks once a merger has been recognized as a likely violation of the law. All the Commissioners agree that this merger is likely to harm competition and violate the antitrust laws; otherwise there would be no need for a consent agreement. The question is what degree of risk that our remedies are insufficient are we to assume. In answering the question, it is reasonable to ask: What are the social benefits of this merger? It is fairly clear that there are no significant "efficiencies" in any ordinary use of the word. While Socal argues that acquiring Gulf will give Socal access to Gulf's technology, few specifics are offered, and Socal's president conceded that Socal can acquire industry technology in other ways. In a survey of possible acquisitions, Socal could not identify synergies with Gulf's upstream assets. Socal's principal basis for any future cost savings appears to be closing down facilities. Based on this and other evidence, the staff concludes that "this acquisition does not present the efficiencies which might have flowed from several earlier mergers in this industry, notwithstanding Socal's statements that it does." In short, I believe the Commission is accepting substantial risks in relying on a complex, uncertain remedy in a case where a merger clearly appears to be unlawful, and offers few, if any, benefits other than to the private parties.

Other Provisions

I am also troubled by a number of other provisions and omissions in the agreement. For example, the agreement provides an option to Socal to divest one of Gulf's two refineries in the Gulf Coast area. Depending on which refinery Socal chooses, the Herfindahl index would still increase about 100 points in kerojet production (less in the case of a divestiture of Port Arthur, more if Alliance is sold). Second, the staff identified an overlap in the sale of aviation gasoline in the Gulf and East coast regions that would exceed the justice guidelines in increasing the Herfindahl index, but did not address it in the agreement. Each of these issues alone would not justify rejecting the entire agreement but, taken together with the considerations mentioned above, they strengthen the argument against it.

Non-Antitrust Issues

However close the antitrust issues are here, and I believe they are closer than in some previous cases on which I disagreed with the majority, we should keep in mind that issues we cannot address under the antitrust laws remain of major, perhaps overriding, importance. This merger is driven by Socal's desire for crude oil. Despite protestations to the contrary by company officials, I find it very difficult to conclude that this merger will not diminish exploration for crude oil. One major company, which has needed additional crude reserves, has now disappeared. A second major competitor, which has had strong incentives to drill, has now won control of 2 billion barrels of crude oil reserves along with a huge debt burden. We may not understand precisely how much this acquisition will reduce exploration but to assume it will affect it little or none at all flies in the face of common sense.

Conclusion

Even though I believe staff has done a commendable job in negotiating this agreement under severe time constraints, in particular, by giving the Commission a greater ability to insure the divestitures achieve their stated purpose, I cannot help but conclude that there are too many unanswered questions and too many risks to endorse this agreement. The law does not require that we go out of our way to restructure acquisitions that violate the antitrust laws, particularly when there is a cloud of uncertainty as to whether our restructuring will or will not work and when the merger, which we are struggling so hard to preserve, offers no significant efficiencies. While the public comment period on this case can be particularly useful, because of the scope and significance of the acquisition and divestitures, I must vote against the agreement based on what has been presented to the Commission.

23624 Federal Register / Vol. 49, No. 111 / Thursday, June 7, 1984 / Proposed Rules

Statement of Commissioner Patricia P. Bailey; Standard Oil of California Acquisition of Gulf Oil Corporation, April 26, 1984

The hold separate and consent agreements tentatively accepted by the Commission in this matter to my mind propose solutions to the measurable, or even reasonably foreseeable anticompetitive consequences of this merger. Substantial divestitures have been ordered, and even additional and contract relief is also available under these agreements, if necessary to facilitate sale of these assets and insure their continuation as competitively viable entities.

Any calculated risk that the relief proposed will not result in the creation of viable new competitive forces in refining and marketing is reduced by a novel requirement that SoCal keep Gulf's domestic petroleum assets as an independent entity until all divestitures acceptable to the Commission have been actually achieved. This means that the Commission maintains substantial legal leverage to insure SoCal's incentive to divest, in accord with the procompetitive injunctions implicit in the Commission's order. I believe that this feature of the relief in this matter will ensure that the Commission can continue to act in the best interests of the public during the divestiture phase of this difficult case.

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The CHAIRMAN. Our next witnesses are Mr. George M. Keller, chairman and chief executive officer of Standard Oil Co. of California, and Mr. James E. Lee, chairman of the board and chief executive officer, Gulf Corp.

We are glad to have you gentlemen here. I presume you have written statements. Now, if it suits you to place them in the record, then you can take about 5 minutes and just tell us in broad, practical layman's terms why you take the positions you do.

STATEMENT OF JAMES E. LEE, CHAIRMAN OF THE BOARD AND CHIEF EXECUTIVE OFFICER, GULF CORP., AND GEORGE M. KELLER, CHAIRMAN AND CHIEF EXECUTIVE OFFICER, STANDARD OIL CO. OF CALIFORNIA

The CHAIRMAN. Mr. Keller, do you want to go first?

Mr. KELLER. I was offering Mr. Lee the opportunity. Why don't you have him go first, if that is acceptable to you.

The CHAIRMAN. Fine.

Mr. LEE. I will go first, if you wish.

Thank you, Mr. Chairman. I am Jim Lee, chairman of the board and chief executive officer of Gulf Corp.

I would like to thank you and your committee for this opportunity to expand upon the letter that I sent you earlier about this merger between Gulf and Standard of California.

Gulf and Socal agreed on this merger 10 days ago, following our board's February 24 decision in principle to explore such a possibility. Both companies made their initial Hart-Scott-Rodino filings March 6.

Now, on Gulf's part, this decision represented the best available alternative to a liquidation plan, which a minority shareholder is trying to impose on us. The Socal offer of $80 per share, in our opinion, is a strong and fair offer to all of our shareholders.

This decision, and those before and after it, was guided by underlying management philosophies to which our directors and I are deeply committed. One is to protect the investment of our stockholders and to increase its value, and another is a commitment to strengthen the energy security of our Nation.

Gulf and Socal are meticulously following the requirements of all applicable statutes and regulations. Both George Keller and I have pledged to resolve any potential antitrust problems. [Laughter.]

All the parties involved in this transaction have followed the rules governing mergers. Now there are proposals to change the rules retroactively. I must tell you that to change them for Gulf,

after the fact, is wrong, and will only have serious undesirable consequences.

Congress should understand that Gulf is currently facing two tender offers: One by Socal, at $80 per share for all of our stock, and another aimed at gaining a controlling interest in our company by buying only some of the shares for $65. The clock is running on both of those offers. And if this Socal offer is delayed as a result of congressional action, the lesser, partial offer of $65 has a good chance of succeeding. That result would be catastrophic for 260,000 shareholders and devastating for 42,000 employees.

Since the strategy behind the partial $65 offer includes a random liquidation of Gulf's assets, it would not be in the best interest of this Nation.

We believe that Socal is committed to a continuation of the strategies to which Gulf has dedicated itself. Gulf has made significant progress in its efforts to implement these strategies for increasing stockholder value and for developing the energy reserves needed by Gulf and the Nation over the long term.

Yet, this progress did not significantly affect Gulf's short-term profitability. Although we were making great strides, market forces and events overtook us. Gulf's stock remained overvalued, and we became the target of a well financed and aggressive group of speculators. And the attention generated by the battle for control of Gulf created such a frenzy on Wall Street that we were finally compelled to recognize that Gulf's survival as an independent company was no longer a viable alternative. Our stock price had been forced up to a point that could not be sustained by current earnings or near-term prospects.

After weighing the alternatives, Gulf's best option was a friendly merger, consistent with our determination to increase stockholder value and to strengthen the Nation's energy security.

Enactment of legislation which would retroactively prohibit the Gulf-Socal merger is bad public policy. Both firms acted responsibly, within the framework of existing laws and chose an action based on the best business judgments of their boards of directors.

If Congress determines that changes are necessary to prohibit speculators from reaping short-term gains by breaking up energy companies in the future, tax law changes now before Congress will help solve that problem. However, legislation to prohibit or delay actions by Gulf and Socal, which were taken in the light of established rules and regulations, will do serious damage to Gulf, to its shareholders, and the ability of the marketplace to provide an efficient domestic energy industry.

The 6-month moratorium contemplated by Senator Johnston's bill would be particularly devastating for Gulf. It would put us in limbo, unable to make major decisions, or capital commitments, or to keep and protect our best employees.

Our merger with Socal provides the best opportunity for our best people to continue their careers as part of a strong, growing, and competitive company.

I strongly recommend that this committee consider whether some legislative action may be appropriate to save other companies from Gulf's fate. But for us, it is just too late. You can only make

Gulf's situation worse, unless it is made clear that our merger with Socal will be excluded from your consideration.

Thank you, sir.

The CHAIRMAN. Thank you, Mr. Lee.

[The following was received for the record:]

TESTIMONY

OF

JAMES E. LEE

CHAIRMAN OF THE BOARD

AND

CHIEF EXECUTIVE OFFICER

GULF CORPORATION

Good afternoon. I'm Jim Lee, Chairman of the Board and Chief Executive Officer of Gulf Corporation. Senator Thurmond, I would like to thank you and your committee for this opportunity to expand upon the letter I sent to you earlier about the merger between Gulf and Standard of California.

Gulf and Socal agreed on this merger ten days ago, following our Board's February 24th decision in principle to explore such a possibility. Both companies made their initial Hart-Scott-Rodino filings the next day. On Gulf's part, that decision represented the best available alternative to a liquidation plan, which a minority shareholder is trying to impose on us. The Socal cash offer of $80 per share, in our opinion, is a strong, fair offer to all of our 260,000 shareholders.

This decision, and those before and after it, was guided by underlying management philosophies to which our directors and I are deeply committed. One is to protect the investment of our stockholders and to increase its value. Another is a commitment to strengthen the energy security of our nation.

Gulf and Socal are meticulously following the requirements of all applicable statutes and regulations. Both George Keller and I have pledged to resolve any potential anti-trust problems. All the parties involved in this transaction have followed the rules governing mergers.

Now, there are proposals to change the rules retroactively. I must tell you that to change them for Gulf, after the fact, is wrong and will only have serious undesirable consequences.

Congress should understand that Gulf is currently facing two tender offers, one by Socal at $80 per share for all of our stock, and another aimed at gaining a controlling interest in our company by buying only some of the shares for $65. The clock is running on both of these offers.

If the Socal $80 offer is delayed as a result of Congressional action, the lesser, partial offer of $65 has a good chance of succeeding. That result would be catastrophic for our 260,000 shareholders and devastating for our 42,000 employees. Since the strategy behind the partial $65 offer includes a random liquidation of Gulf assets, it would not be in the best interests of the nation.

We believe that Socal is committed to a continuation of the strategies to which Gulf has dedicated itself. Gulf has made significant progress in its efforts to implement these strategies for increasing stockholder value and for developing the energy reserves needed by Gulf and the nation over the long term.

Yet, this progress did not significantly affect Gulf's short-term profitability. Although we were making great strides, market forces and events overtook us. Gulf stock remained undervalued, and we became the target of a well-financed and aggressive group of speculators.

The attention generated by the battle for control of Gulf created such a frenzy on Wall Street that we were finally compelled to recognize that Gulf's survival as an independent company was no longer a viable alternative. Our stock price had been forced up to a point that could

not be sustained by current earnings or near term prospects. After weighing the alternatives, Gulf's best option was a friendly merger consistent with our determination to increase stockholder value and strengthen the nation's energy security.

With this uppermost in our minds, our Board decided ten days ago that the merger offer presented by Standard Oil Company of California best served Gulf stockholders, employees, customers, and the nation. As George Keller assured the committee in his statement, Gulf's jobbers, retail dealers, and customers will continue to have access to an adequate supply of petroleum products through the transition period. All of Gulf's current supply contracts with jobbers and dealers will be honored, consistent with FTC requirements.

Enactment of legislation which would retroactively prohibit the Gulf/Socal merger is bad public policy. Both firms acted responsibly, within the framework of existing laws, and chose an action based on the best business judgements of their boards of directors.

If Congress determines that changes are necessary to prohibit speculators from reaping short-term gains by breaking up energy companies in the future, tax law changes now before Congress will help solve that problem. However, legislation to prohibit or delay actions by Gulf and Socal, which were taken in light of established rules and regulations, will do serious damage to Gulf, its shareholders and the ability of the marketplace to provide an efficient domestic energy industry.

The six-month moratorium contemplated by Senator Johnston's bill would be particularly devastating for Gulf. It would put us in limbo, unable to make major decisions or capital commitments, or to keep and protect our best employees. Our merger with Socal provides the best opportunity for our best people to continue their careers as part of a strong, growing and competitive company.

Gulf's survival is no longer a viable alternative. Gulf has been sold by the marketplace; and the sale will either take place through the merger with Socal, the Mesa Group's tender offer, or as the result of a proxy contest that would force the company's liquidation. Obviously the Socal merger is the best — indeed the only one — of these alternatives. It provides cash to all of our shareholders for all of our stock. It prevents the random liquidation of Gulf's assets. It protects jobbers, dealers, and customers. It assures continued employment for most of our employees.

I strongly recommend that this Committee consider whether some legislative action may be appropriate to save other companies from Gulf's fate. But for us it is just too late. You can only make Gulf's situation worse unless it is made clear that our merger with Socal will be excluded from your considerations.

The CHAIRMAN. Mr. Keller, please proceed.

Mr. KELLER. Thank you, Senator.

My name is George M. Keller. I am chairman and chief executive officer of Standard Oil Co. of California. I am here at the invitation of the committee to provide any information I can about the merger of Standard Oil Co. of California and Gulf Corporation.

I appreciate the opportunity to appear before the committee today. I believe we can show the committee that this is an excellent merger and that it will greatly benefit the Nation, as well as the parties involved. My reasons are as follows:

The merger will bring together the exploration and producing resources of our two companies in a new combination that we believe will be greater than the sum of its parts. We believe it will result in a more effective exploratory program both in the United States and abroad, than the one our companies could have carried forward individually.

The merger will provide for a reorientation of Gulf's refining and marketing operations, in a way that offers the best opportunity to preserve their viability as going businesses.

The merger will preserve more jobs than any other realistic alternative.

The merger will preserve the competitiveness of the existing industry structure.

The merger will not significantly affect either the cost or availability of credit.

I have submitted to the committee a prepared statement, which I believe you all have. I will not repeat that testimony now.

I would like, however, to tell you briefly why I believe this merger is very much in the national interest.

First, I believe this merger will strengthen the Nation's search for oil and gas reserves. A major challenge facing the oil industry in the United States today is to find and develop additional petroleum reserves. I am sure I need not remind this committee that our Nation is too dependent on petroleum supplies from abroad. I am sure the committee also knows that U.S. oil and gas reserves have been declining for many years.

This merger will bring together Socal's and Gulf's technical and human resources in a new combination that we believe will provide a more effective program of exploration than the companies are carrying on today.

We in Socal plan to carry on an exploratory program comparable in effort to the combined programs of the two companies—a program far greater than would occur if Gulf operations were liquidated, which is the only alternative to this merger.

We will continue to concentrate on the high-cost, high-risk, frontier areas, where the larger oil and gas fields remain to be found.

Second, I believe the merger will provide for the reorientation of Gulf's refining and marketing operations in a way that will provide the best opportunity to preserve their viability as going businesses. Oil demand in the United States peaked at nearly 19 million barrels a day in 1978. It declined to about 15 million barrels a day in 1983. Obviously, this means that the United States has a good deal more refining and marketing capacity than it needs. Therefore, the industry will have to move toward some degree of consolidation. We believe our merger with Gulf provides the best opportunity to maintain Gulf's viable refining and marketing operations as going businesses.

Third, we believe the merger will preserve more jobs than any other alternative available. We believe that Gulf as a going concern has a value in excess of the value of its assets alone. We do not yet know what parts of Gulf we will be permitted by the Federal Trade Commission to bring into our company, but we hope to preserve as much of Gulf as possible as a going operation, whether as part of our own or some other company's operation. We believe that this merger will preserve strong competition in the oil industry. The oil industry is widely known for its absence of economic concentration. The present competitive situation will not be affected significantly by the merger.

Prof. Edward Mitchell, of the University of Michigan, who is here with me today, is an expert on the subject of competition in the oil industry. He has submitted a written statement and will be glad to testify if the committee wishes.

We believe this merger will not have any significant effect on the cost or availability of credit in the United States. It will bring some $2 billion into Federal and State treasuries, because of taxes on gains realized by Gulf shareholders. However, we believe Gulf shareholders will continue to regard most of the rest of the $13.2 billion as capital, and reinvest it in the capital markets.

No doubt oil and gas exploration and production ventures will get their share. The taxpayers do not underwrite this financial undertaking. Interest income is taxable to the recipient.

Mr. Leif Olsen, chairman of the economic policy committee of Citibank, who is here with me today, is an expert on this subject. He has prepared a statement and will be glad to testify if the committee wishes.

I would like to assure the committee and Gulf's jobbers, retail dealers, and customers that we will assist Gulf in protecting them as much as possible. All of Gulf's current supply contracts with jobbers, dealers, and customers will be honored by Gulf and Socal, consistent with FTC requirements. Our companies will also attempt to assure, insofar as we reasonably can, that all of Gulf's jobbers, dealers, and customers continue to have access to an adequate supply of petroleum products.

If I may continue for a moment, finally, I would like to comment on what seems to me the key issue before the committee today—that is, are the interests of all the parties and the national interests better served by a merger between Socal and Gulf, or are they better served by having Gulf taken over in a hostile merger and liquidated.

Other theoretical alternatives may be of interest to discuss, but these are the two that exist.

The CHAIRMAN. Mr. Keller, do you wish your entire statement to go in the record?

Mr. KELLER. Yes, I do, please.

The CHAIRMAN. Fine. We thank you both for your presence.

[The following was received for the record:]

STATEMENT OF MR. GEORGE M. KELLER
CHAIRMAN AND CHIEF EXECUTIVE OFFICER
STANDARD OIL COMPANY OF CALIFORNIA

My name is George M. Keller. I am Chairman and Chief Executive Officer of Standard Oil Company of California. Mr. Edward Mitchell, Professor of Economics at the University of Michigan, and Mr. Leif Olsen, Chairman of the Economic Policy Committee of Citibank are here with me.

I am here at the invitation of the committee to provide any information I can about the merger of Standard Oil Company of California and Gulf Corporation.

I appreciate the opportunity to appear before the committee today. I believe we can show the committee that this is an excellent merger which will greatly benefit the nation as well as the parties involved. My reasons are as follows:

- The merger will bring together the exploration and producing resources of our two companies in a new combination that we believe will be greater than the sum of its parts. We believe it will result in a more effective exploratory program, both in the United States and abroad. We plan to continue an exploratory program comparable in effort to the total of the programs our two companies would have carried forward individually. However, we hope the program will be even more effective because of the stimulating effects of combining our technical and research organizations.

- The merger will provide for a reorientation of Gulf's refining and marketing operations in a way that offers the best opportunity to preserve their viability as going businesses.

- The merger will preserve more jobs than any other realistic alternative.

- The merger will preserve the competitiveness of the existing industry structure. The oil industry is widely known for its absence of economic concentration. This will not be significantly affected by the merger.

- The merger will not significantly affect either the cost or the availability of credit.

We believe that mergers are in the national interest provided they meet the test of antitrust limitations required by existing legislation. New laws prohibiting or delaying friendly mergers that do not adversely affect competition would be a serious mistake.

As Assistant Attorney General, J. Paul McGrath, said in a speech last week,

> "Government merger policy strongly affects the economy. The free movement of business assets is critical to economic growth. For that reason, business managers must be free from irrational antitrust constraints in deciding whether to acquire or divest businesses. Antitrust enforcers should only block mergers when they conclude, based on sound economic analysis, that a particular transaction will adversely affect competition."

The committee is aware that the FTC is studying the merger to see if there are any adverse competitive consequences. We filed our Hart-Scott-Rodino pre-merger notification on March 6. The FTC has asked us for additional information, and we have met their initial requests. We are cooperating fully with the FTC. We will do whatever may reasonably be required to meet any antitrust concerns.

I hope very much that the Congress will not enact legislation to delay the completion of this merger beyond the time required for these negotiations.

Such delay would pose special problems. On March 5, 1984, Socal entered into a merger agreement with Gulf. Our Merger Agreement with Gulf is not a proposal or an agreement in principle, but a binding contract. This agreement was entered into by the Boards of Directors of both companies acting in good faith and advised by counsel based on existing law. Pendency of this or any other legislation does not relieve Socal of this contractual obligation. Once the antitrust clearance process is completed, we are legally obligated to purchase the Gulf shares for $13.2 billion in cash. If the bill is enacted after our purchase, its retroactive nature would create the most complex legal and financial dilemma in corporate history. This transaction cannot be unwound. Socal would be faced with the apparent prospect of being forced by the legislation's retroactive effective date to divest the purchased assets with potentially fatal financial consequences for the Company and its shareholders.

Since the announcement of our contract with Gulf, over a billion dollars of Socal and Gulf stock have been traded on the nation's securities markets in reliance upon the terms of the merger agreement. Gulf has over 200,000 individual and institutional stockholders, most of whom are not in a position to follow and analyze legislative developments of this nature. To enact retroactive legislation after trading of this magnitude has occurred would not only be unfair to these investors but would introduce an unprecedented destabilizing factor to the nation's capital markets. The fairness and equity of the rules governing our capital markets will be in question if the transaction is jeopardized by the retroactive application of an act of Congress.

Finally, the proposed legislation in its present form assumes that Gulf could otherwise survive as a viable, independent company. This alternative is no longer realistic under the circumstances. There are only two roads for Gulf now: acquisition by Socal or liquidation. Even if the moratorium were to be enacted, Gulf and other oil companies covered by the proposed legislation would still be vulnerable to proxy fights to force liquidation. We understand that the so-called Gulf Investor Group headed by T. Boone Pickens is planning such a proxy contest in the immediate future.

Mr. James E. Lee, Gulf's Chairman and Chief Executive Officer is here today and could well testify to the inequities retroactive application of this legislation would impose.

I am here today to provide any information I can on the merger. I welcome the opportunity to correct a number of misapprehensions and misunderstandings that appear to exist. I do not, however, consider myself an authority on mergers other companies have made or may make in the future. I plan, therefore, to confine my remarks to the facts surrounding our merger with Gulf.

I should like today to testify on four subjects:

- The role of mergers in our economy.
- Socal's merger with Gulf.
- How Socal plans to implement the merger with Gulf.
- Effects of the merger on Socal's and Gulf's employees, stockholders, jobbers, dealers, and customers; on credit markets; and on the national interest.

The Role of Mergers in our Economy

Most economists believe that mergers are a normal and healthy part of our free economy. They are a means whereby companies become more efficient, thus benefiting the consumer. They are also a means whereby the nation's resources of capital and manpower are constantly assessed and redeployed to the most productive uses in our changing economy. This process is not without risk to the managements of the companies involved. Recent events in the oil and other industries show that even the managements of very large companies - probably including my own - are not immune. However, I believe this represents a healthy process of competition and renewal which the Congress should encourage.

A number of recent mergers have involved oil companies. I believe several conditions have come together to bring this about.

The first is the increasing difficulty and cost of finding oil. I said publicly two years ago that I believed we in Socal could find and develop oil and gas reserves more cheaply than we could buy them. I am not sure that is true today, particularly in the United States. We have in our company what I believe is one of the most efficient and successful exploration organizations in the oil business. Nevertheless, our oil and gas reserves have been gradually declining. The difficulty and cost of finding oil has increased rapidly in recent years for several reasons.

- First, the onshore Continental U.S. has been pretty extensively prospected. While many more worthwhile reserves of oil and gas will be found onshore and offshore in the U.S., it seems likely that most large oil and gas fields will be found in higher-risk, higher-cost frontier areas. Even in these areas, recent exploratory results have been disappointing, as the dry hole at Mukluk on Alaska's North Slope showed.

- Second, actions by the United States government - and, to some extent, other levels of government - have withdrawn large areas of government land from exploration. As an example, some 85% of the California offshore area is now off limits to oil and gas exploration because of moratoria. Thus government has put off limits some of the more promising areas where the industry was hoping to discover more oil and gas.

- Third, host country governments in foreign countries where we try to negotiate exploratory concessions are making demands that often make it uneconomic to do business. And even those terms are often later renegotiated upward to our detriment in countries where exploratory efforts are successful. Host governments in some cases have taken over our operations entirely.

It is for these reasons, as well as a view that oil prices will not increase in the medium term, that the count of active rigs has decreased from over 4,500 in 1981 to under 2,500 today.

Nevertheless, we are continuing to carry forward a very large exploratory program. We currently have active exploration operations in 21 states and 38 foreign countries. As I said earlier, we plan to continue a major exploratory program comparable in effort to the total of what our two companies have been carrying forward separately.

At this point, I would like to put to rest the concern of those who see this merger as merely "drilling for oil on Wall Street." It is far from that. I am enormously proud of my company's technical capability and track record as a leader in exploration for oil and gas, and in the research that supports this program. This capability, combined with the resources of Gulf and the financial strength of the merged operations, will be applied to Gulf's extensive reserves and land holdings. As a result, we

will be able to carry out an outstanding exploration program that will combine the resources of both companies.

Beyond what we can accomplish by our own strong exploratory program, we are constantly looking for opportunities to add to our oil and gas reserves in other ways.

This brings me to the second reason why a number of oil company mergers have taken place in recent years. That is, the depressed price of the common stock of many oil companies. These shares are depressed for several reasons:

- First, there is a general belief that demand for oil will be flat, or perhaps even decline, for the indefinite future.

- Second, there is a great deal of excess refining and marketing capacity in the industry which must be consolidated if consumers are to be served efficiently.

- And finally, there is a very large surplus of oil producing capacity around the world today.

Thus there is a general belief that there will be surplus capacity worldwide in producing, refining and marketing for many years. This has depressed the price of oil company shares.

However, we, and apparently some others, believe that the true value of the shares of some of these companies is considerably greater than the value the market now places on them. Thus, we have been alert for some time to the possibility that we might be invited to participate in a friendly merger that would result in increasing our shareholders' values at an attractive price.

In addition to the increasing difficulty and cost of finding reserves, and low current market prices for oil company stocks, I

should mention one final factor that I believe currently encourages mergers. That is the practice of some companies of pursuing acquisitions with the intent of liquidating the companies they acquire. Companies that are pursued by other companies intent on their liquidation have a strong incentive to negotiate a friendly merger with a company like Socal.

Socal's Merger With Gulf

As I indicated above, our company has for some time been examining the benefits of a friendly merger with another oil company. We have evaluated a number of possible partners and tried to determine a fair price. Gulf was among the companies we studied. However, we did not participate publicly in any bidding "contest" for a merger partner.

On February 24 I received a telephone call from Mr. James E. Lee, Chairman of the Board and Chief Executive Officer of Gulf Corporation. On behalf of the Gulf Board, Mr. Lee inquired whether Socal would be interested in pursuing a friendly merger with Gulf. I replied that we would. Over the next ten days, several of our people met with Gulf's people to develop information. On the morning of March 5, I presented our company's offer to the Gulf Board of Directors. Other interests also presented offers at that time. I was advised during the afternoon of March 5 that our offer had been accepted by Gulf's Board.

Our offer provides for the friendly merger of the two companies through a cash purchase of Gulf's shares by Socal. Under the agreement, Socal will make a tender offer for all the outstanding shares of Gulf's common stock at $80 per share. Socal is not obligated to purchase shares under this offer unless a minimum of 85 million shares (about 51% of the outstanding shares) are

tendered. Other terms and conditions are set forth in the agreement, which I will be glad to make available to the committee.

We see the merger as having a number of advantages for Socal:

- It was made on a friendly basis, in response to an invitation from Gulf. Thus, we look forward to good and productive relationships with Gulf's management and employees.

- It substantially increases our company's assets - particularly oil and gas reserves - at an attractive price.

- The merged companies are an excellent match geographically and functionally in most important categories. In terms of oil and gas reserves, both Socal and Gulf are active in the North Sea. Socal has a major position in Indonesia, Australia, and the Sudan, and has important historic ties in Saudi Arabia, while Gulf's other foreign activities are concentrated in West Africa. Domestically, Socal is an industry leader in exploration in California, Louisiana, and in the Wyoming Overthrust area. Gulf is strong in Texas, and both have significant operations in the Gulf of Mexico. In marketing, Socal is the largest gasoline marketer in the Southeast and Western part of the U.S. Gulf is strongly represented in the Northeast and Southeast.

- The merger creates one of the world's strongest energy firms, technically and financially able to compete more efficiently in the domestic and international petroleum business.

  Technical research on how to find and produce oil more effectively will be a key to increasing the nation's oil

and gas supplies in the years ahead. We believe the combination of Socal's and Gulf's advanced research resources will enable us to show outstanding results.

The increasing costs and risks of developing reserves in frontier areas, both in the United States and abroad, require that companies be larger and stronger technically and financially if they are to explore and develop these prospects. Large companies serve the national interest in developing frontier areas. It is also clearly in the national interest to have companies that are strong enough to compete with large foreign oil companies - many supported by their governments - in acquiring and developing concessions abroad.

We believe the merger offers many advantages to Gulf Corporation as well. As I said before Mr. Lee is here today, and I believe it would be appropriate for him to testify on that subject.

How Socal Plans to Implement the Merger With Gulf

As I indicated above, our merger agreement with Gulf was signed on March 5, only ten days ago. I hope, therefore, that the members of the committee will understand if I am not able at this time to provide a detailed plan on how we will proceed from here.

We have, however, developed some guidelines that we believe will result in an efficient and humane redeployment of Gulf's assets and people.

- We believe that Gulf has a value as a going concern in excess of the value of its assets alone. We mean to protect this value by maintaining Gulf's operations as going concerns until they are integrated with our own operations or absorbed into some other company's operations.

- Socal may be required to divest itself of some of Gulf's refining and marketing properties in order to comply with the antitrust laws. We plan to work with the Federal Trade Commission and other government agencies to do whatever is reasonably required to be in compliance.

- If it becomes necessary to divest facilities and the people related to them, we believe it is desirable to do so in "packages" designed to be commercially viable, rather than in pieces that may not have the strength to survive. To do this we may divest some additional parts of Gulf beyond those required to comply with antitrust laws.

- So far as we know, there are no antitrust problems associated with merging all of Gulf's exploration and producing operations with ours. As I indicated earlier, we expect to have an exploration program in Socal that will be comparable in effort to our two companies' operations now. We hope this program will be even more effective because of the combination of Gulf's and our own technical resources. We view the acquisition of Gulf's reserves as an addition to a very strong ongoing exploration program.

- Gulf Corporation has been negotiating for the sale of its 60% interest in Gulf Canada. We will continue these negotiations.

- We have not had the opportunity to determine how Gulf's coal, chemical and nuclear operations may fit with Socal's operations. We will be giving this careful study as soon as possible.

Effects of the Merger

I would like to say a word about the people involved in the merger. Mergers of this kind inevitably involve some

consolidation of operations. Also, a spin-off of some of Gulf's operations may be required by the FTC to comply with the antitrust laws.

It is impossible to know now just how employees will be affected. But I would like to assure the committee - as well as Gulf's employees - that we will do all we can to make whatever changes are required with full consideration for the lives of the people involved. Our company has a long-standing reputation for treating its people well, and for handling people involved in organizational changes of this kind with consideration. We value this reputation, and we intend to handle this merger in a way that will entitle us to keep it.

I would also like to comment on the impact of the merger on Gulf's jobbers, retail dealers, and customers. Gulf serves gasoline markets in 26 states. As with other aspects of the merger, it is impossible now to say exactly what arrangements will be made with respect to these operations. But I would like to assure the committee - as well as Gulf's jobbers, retail dealers, and customers - that we will attempt to assure insofar as we reasonably can that they will continue to have access to an adequate supply of petroleum products throughout the transition period. All of Gulf's current supply contracts with jobbers and dealers will be honored by Gulf and Socal consistent with FTC requirements.

The impact of a merger on competition is, of course, a matter of public concern. The petroleum industry is well-known for its absence of economic concentration. After our merger with Gulf we will represent about 7% of U.S. oil production, 14% of U.S. refinery capacity, and 11% of U.S. petroleum product sales. These are hardly numbers to cause concern. The latter two percentages will be smaller if the FTC requires us to divest ourselves of some of Gulf's refining and marketing operations.

One should not, of course, simply look at the size of a company to judge the state of competition in an industry. Oil companies are large because vast amounts of capital are needed to find and develop reserves of oil and gas, to refine crude oil into useful products, and to make it available wherever it is needed.

Oil companies are large because the energy needs of the nation are large. The value of petroleum products shipped from this nation's refineries amounts to over half a billion dollars a day, or nearly three times the value of the cars and trucks shipped daily from our automobile factories.

Moreover, U.S. oil companies compete against very large oil companies headquartered abroad, many of which are backed by the resources of their governments. It is interesting to note that Japan has recently discussed requiring a number of its oil companies to combine so that each group will have a minimum of 10% of the market. Similar trends toward increasing size can be seen in other foreign oil companies.

I am not, as the committee knows, a professional expert on the subject of industry size or competition. As I mentioned earlier, Professor Edward Mitchell, who is here today, is such an expert. He has submitted a statement on this subject and will be glad to testify if the committee wishes.

I would also like to comment on the concern that Socal's borrowing in connection with the merger will deprive other borrowers of credit and drive interest rates up.

We believe Socal's borrowing for the merger will have a negligible effect on the credit markets, even if we borrow the entire $13.2 billion required.

Gulf's shareholders will pay federal and state taxes on the $13.2 billion they receive. Of course, we do not know the exact amount of taxes that will be paid, but they will probably be

approximately $2 billion. These taxes will reduce government borrowing, so they will not add to credit demand. The rest of the $13.2 billion will continue to be regarded by Gulf shareholders as capital, and will be reinvested in the capital markets, including oil exploration and production ventures. Acquisitions, whether they are made for stock or cash, do not destroy capital. The capital is still there. The stockholder is not going to put the cash he receives from this merger in the attic and take it out of circulation. He is going to reinvest it. The proceeds will remain a part of the nation's capital resources, available to meet other capital needs.

As I mentioned earlier, Mr. Leif Olsen, Chairman of the Economic Policy Committee of Citibank, is here today. He has submitted a prepared statement on this subject and will be glad to testify if the committee wishes.

There also seems to be some feeling that a merger between oil companies should be viewed with particular suspicion because of a general misunderstanding that all oil companies are unusually profitable. I wish this were true. The fact is, however, that the average rate of return on equity for U.S. industry as a whole in 1982, the most recent year available, was 11.0%. The figure for Socal was 10.6%, and for Gulf 9.1%. The relationship is similar if one measures the return on capital employed. Thus Socal and Gulf were slightly less profitable than U.S. business as a whole.

It seems to me particularly inappropriate, therefore, for the Congress to consider legislation aimed at the petroleum industry alone, such as recent bills that would bar oil company mergers. In my view, this represents an invidious discrimination against one industry, and an industry which is essential to the nation's security and well-being. Perhaps more important, it discriminates against a particular group of shareholder-citizens, including millions whose retirement funds are invested in part in oil company securities. It should also be noted that legislation

of this kind would not prevent hostile acquisitions and liquidations.

The oil industry is going through an inevitable restructuring as it tries to respond to today's economic environment and move toward a more viable structure. Any restraints imposed by government will inject artificial influences into this process.

This will result in an oil industry much less efficient and less able to serve the national interest and meet the nation's energy requirements. The bills proposed to curb these normal developments of the economic system would have disruptive results not unlike those that followed the government's attempts to legislate so-called "fair" distribution of petroleum supplies during the 1973 shortage.

Conclusion

I would like to close by commenting on what seems to me to be the key issue we should concentrate on here today. That is, whether the interests of all the parties concerned and the national interest are better served by a merger between Socal and Gulf, or whether they are better served by having Gulf taken over in a hostile acquisition and liquidated. Other theoretical alternatives may be of interest to discuss, but these are the two that exist.

In my view, it is clear that the interests of all concerned are better served by the merger. As I said earlier, the Socal-Gulf merger will result in an exploratory program of at least the same level of effort as the combined programs of the two companies before the merger, strengthened by the stimulating effects of combining our technical and research resources. Gulf's refining

and marketing organizations will be operated as going businesses until they are merged into Socal or reoriented in new directions. The people affected by the merger will be provided for in keeping with Socal's long-standing personnel practices. And Gulf's jobbers, dealers, and customers will be assured that Gulf's contracts will be honored and that they will have a reliable supply of petroleum products during the transition period. If this is contrasted with what would happen in each of these areas if Gulf were the victim of a hostile takeover and liquidation, I believe the answer is clear.

I will be glad to answer any questions the committee may have.

STATEMENT OF

PROFESSOR EDWARD J. MITCHELL

GRADUATE SCHOOL OF BUSINESS ADMINISTRATION

UNIVERSITY OF MICHIGAN

Mr. Chairman and members of the committee. My name is Edward Mitchell. I am Professor of Business Economics at the Graduate School of Business Administration of the University of Michigan. I appear before you today with Mr. George Keller, Chairman of the Standard Oil Company of California (Socal). The views expressed by me in this statement reflect only my personal views on the subject of these hearings and may not reflect those of Socal or of my University.

The issue raised by these hearings, as I understand it, is whether or not there are special aspects of the Socal-Gulf merger or other recent oil company mergers that require government actions beyond the normal antitrust investigation now being carried out by the Federal Trade Commission. My view is that there are no considerations unique to these mergers that should lift them out of the usual antitrust process and that require the attention of the Congress. My statement focuses on specific arguments raised against recent oil company mergers and on the consequences of restricting them.

* * * * * * * * * * *

What makes a market economy so productive is the freedom of individuals and businesses to make decisions based on the unique knowledge they possess of the alternatives. These decisions include (among many others) what consumers choose to buy, where workers choose to work, and what businesses choose to invest in. It has been the philosophy of our social system that restrictions on these decisions are presumptively wasteful and counterproductive

unless one of two special considerations is involved: the presence or potential of monopoly, or the existence of side effects -- for example, air or water pollution -- on parties not consulted in these private decisions.

The experience of the oil industry since 1971 is eloquent testimony to the havoc caused by intervention that is based not on sound principles of public policy, but on half-baked ideas and momentary passions. Some of the mistakes of the 1970s include:

-- shortages of gasoline and long lines at the gas station caused by price and allocation programs;

-- wasteful investment in inefficient refineries caused by the entitlements program;

-- increased dependence on insecure imported oil caused by price regulation of oil and gas.

In each case policy makers believed they could somehow improve the well-being of American consumers by altering the decisions that would otherwise be made by oil company managers.

Contrast this period with the three years since oil decontrol in 1981. Prices have fallen, supplies are abundant, and uneconomic facilities, especially refineries, have been retired or put to better use.

I would think this history would at least give pause to those who operate under the presumption that oil industry executives need a great deal of help from Washington in deciding how to make their investments.

Some Popular Fallacies Regarding Mergers

The principal function of management is to invest their stockholders' assets in the most productive way possible. One set of choices that continuously confronts management is whether to create new assets, purchase existing assets from someone else, or sell existing assets to someone else. The decision rule for each is the same: do

what is most economical. If one can acquire existing assets cheaper than new ones, buy them. If one can realize more money from selling assets than from keeping them, sell them.

There seems to have arisen in popular discussion the idea that purchasing existing assets is somehow economically inferior to creating new ones. The notion is, I suppose, that if someone chooses to buy an existing asset instead of a new one, less new ones will be produced, and hence new investment in the economy will be reduced.

This reasoning is incorrect. Perhaps the best way of understanding the error is to consider the largest investment that families typically make: their own homes.

Families always have a choice of whether to buy an existing home, or have a new one built for them. If they choose an existing home this does not change the total demand for housing in the country. If the demand for housing exceeds the number of homes that already exist no amount of sales and resales of the existing stock of homes will satisfy the demand. At some point someone, either a new buyer or the recent seller of an existing home, will choose to have a new home built. They will do this because the continual bidding up of the price of the inadequate number of existing homes will make building a new home more attractive. Thus, the choice of one particular buyer between new and used does not affect the number of new homes built.

It is also obvious from this metaphor that borrowing money from the bank to finance the purchase of the existing home does not deplete the amount of money available to build new homes, or to invest in the economy generally. The seller of the existing home obtains the proceeds of the sale. Typically, he will use the funds to buy another existing home or to build a new one. If he builds a new one the original bank loan winds up financing a new home. If he buys an existing home, the seller of that home winds up with

the money from the bank loan. I think it is easy to see that if there are not enough homes to satisfy the demand all of the additional bank loans in the economy actually wind up financing newly built homes. Again, the decision by any family to build a new home or buy an existing one has no real effect upon the number of homes built, nor on the capital available for other investments in the economy.

The same metaphor explains why it would be a terrible idea to restrict the purchase or sale of existing assets. Suppose a law were passed that made it difficult to purchase or sell an existing house, the motive being to encourage the building of new homes. Families would make the following calculations: the cost of a house depends upon the initial purchase price and the costs of upkeep; the benefits of a house depend upon the value of living in it each year and the expected amount it can be sold for in the future. Clearly if the resale of your house will be restricted in the future, whether you built it or bought an existing house, the future sales price will be expected to be lower and therefore the attractiveness of investing in houses, used or new, will be diminished. Immediately there would be a drop in the price of existing houses to reflect their lower future worth. Fewer, not more, houses would be built.

If restricted in buying and selling homes we would also find that families would not end up in the houses they preferred to live in.

The lessons for the oil industry merger issue are clear:

-- the choice by any one business to purchase existing assets instead of investing in new ones does not affect the amount of new investment.

-- bank loans made to finance acquisitions do not disappear from the economy; the sellers receive the funds and they are available for

new investment in the oil industry or any other industry; the amount invested in oil exploration, for example, depends only on the price of oil (which is set outside the United States) and the exploration prospects available in the United States.

-- restrictions on mergers or acquisitions in the oil industry would reduce the amount invested in the oil industry, that is, in crude and natural gas production, refining, marketing, etc.

-- restrictions on mergers or acquisitions would also mean that industry assets would not wind up in the hands of the managements that could make the best use of them.

The Affirmative Case for Mergers

Mergers offer significant benefits to the economy if certain efficiencies can be gained. Potential economies from mergers include:

-- scale economies, the larger size of the merging firms permits lower costs of production.

-- the marriage of complementary factors, e.g., a firm with strong new product R & D merges with a firm strong in marketing.

-- the rationalization of production facilities, e.g., two firms vertically integrated into the same businesses find that shutting down the weakest units in the chain in each firm enable the merged firm to operate only the most efficient units.

-- replacement of weak management, so that assets can be employed more efficiently.

-- the economical transfer of technology where the cost of transfer between firms may be prohibitive.

Sometimes the benefits of mergers can be achieved merely by their threat as, for example, when weak management arranges its own reform to avoid its complete removal in the case of merger or acquisition.

There is evidence that the Socal acquisition of Gulf involves the potential for significant efficiencies. Based on estimates from the Value Line Investment Survey, the rate of return on assets earned by Gulf in 1983 was 8.5 percent. For the integrated petroleum industry as a whole it was 10.5 percent. For Standard Oil of California it was 12.0 percent. This would appear to offer a potential for improvement in the utilization of Gulf's assets.

The Competitive Aspects of Mergers

The legitimate concern about mergers is that they increase the chance of monopolization. In the present case -- Socal-Gulf - that chance is nil. In crude oil reserves or production the newly created firm would represent but a small piece of a world crude oil market dominated by the principal OPEC producers. The Socal-Gulf combined crude production amounts to something akin to 4 percent of world production.

Based on 1982 data on U.S. crude oil reserves, after the Socal-Gulf and Texaco-Getty mergers concentration would rise from 29.8% to 30.0% at the 4-firm level and move from just 44.5 percent to 49.3 percent at the 8-firm level.

Based on 1982 data, Socal and Gulf rank tenth and eleventh in U.S. natural gas reserves. Their merger, together with that of Texaco-Getty would raise the four-firm concentration ratio from 23.4 percent to 24.3 percent and the eight-firm ratio from 35.7 percent to 37.5 percent, both very small changes to numbers that are already small.

In some parts of the country the merger of the refining and marketing assets of Socal and Gulf could result in more significant increases in concentration. Chairman Keller has already announced that Socal is prepared to

divest itself of whatever Gulf refining and marketing assets are necessary to gain approval of the merger from the Federal Trade Commission. It is difficult to see under these circumstances how any anticompetitive effects would follow.

The Significance of Some Political Reactions

If the oil industry were heavily concentrated and the recently announced mergers would enhance the monopoly power of the larger firms the merger announcements would have been greeted with the silent applause of the smaller firms in the industry. The reason is that the exercise of monopoly power would involve lower production from the larger firms in order to support higher prices. The small firms would benefit most from these mergers. They would sell more than they do now at even higher prices.

Judging from press reports this has not been the political reaction of smaller firms. Rather they appear to have mobilized some congressional opposition to the mergers. This can only mean that the merged firms are regarded as potentially more serious competitors, presumably because the new combinations will be more efficient.

We conclude that some smaller oil companies, who are in an excellent position to judge the consequences of the mergers, regard them as essentially pro-competitive.

(I dismiss the idea that small oil companies fear predatory tactics of the larger oil companies. These claims have been made for so long without supporting evidence and with enough contradictory evidence that they no longer deserve a serious hearing.)

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In summary, I see no special circumstances in these mergers that would suggest intervention beyond the normal investigation and clearance by antitrust authorities. On the contrary the potential efficiencies from the mergers and the negative effects that restrictions to this or other recently announced mergers would have make it imperative that we grant these mergers the lack of attention they deserve.

Leif H. Olsen
Chairman Economic Policy Committee
Citibank, N.A.

My name is Leif H. Olsen, and I am the chairman of the economic policy committee of Citibank. I am pleased to have this opportunity to share some thoughts on the ability of the financial markets to accommodate the acquisition of the Gulf Oil Corporation by Standard Oil Company of California.

Conclusion

Standard Oil Company's borrowing of $13.2 billion from more than 60 commercial banks to purchase Gulf Oil would not increase interest rates and, even if participants in the market believed it would, the resulting rate rise would be very small and very brief. And the borrowing by SOCAL would not withhold credit from competing borrowers. It is a financial transaction in which shareholders receive cash in exchange for their equity shares, something that happens every day as shareholders around the world buy and sell billions of dollars worth of shares in U.S. corporations. This transaction is different only in that it involves the purchase of all the shares of a single company — Gulf Oil Corporation. A $13.2 billion transaction may seem large in absolute terms but when placed in the context of the $1 trillion gross transactions undertaken in the equity market last year, it represents less than 1 1/2%. Compared with gross bank lending and investing of more than $4 trillion, it represents one third of one per cent.

When it is placed in the context of net additional new credit, which last year amounted to $510 billion and this year is targeted by the Fed at $470-570 billion, it is 2.5% of that total. But it is not appropriate to look at this as a net addition to total outstanding credit, as might be the case if the borrowed money is used to acquire real new capital, whether it be brick and mortar and machinery or new automobiles and houses. The SOCAL acquisition of Gulf Oil is, instead, a purely financial transaction in which the borrowed money would pass swiftly to the shareholders of Gulf. They would then use those proceeds to buy other stocks or bonds. So given the fungibility of money, the proceeds from the Gulf purchase by SOCAL would flow back into the money markets where they would be available to finance business. No credit is withheld from other borrowers, and the effects on interest rates, if any, are very small and shortlived and would arise only from the illusory expectations of market participants. Furthermore, that part of the $13.2 billion received by Gulf share-

holders which is paid in taxes (perhaps about $2 billion) will offset the need for an equivalent amount of borrowing by the federal government.

Why Interest Rates Move

The demand for credit is a widely misused concept. Whenever there is a rise in the volume of credit extended, it is described by the press — and often by economists — as an increase in credit demand. But such a statement ignores the supply side of the credit market. Increases in the volume can — and often do — stem from an increase in the amount supplied. That is what happens when interest rates fall as the volume of credit extended increases. And it actually did happen in 1982. On the other hand, if interest rates rise in the face of an increase of volume, then it is clear that demand has outpaced supply.

Interest rates — the price for credit — rise or fall in response to changes in supply and demand. Total demand in the private sector is determined by the income expectations (including inflation) of borrowers, households as well as businesses. If nominal income is expected to rise, credit demands will rise. Interest rates in such a situation are also likely to rise if inflation is expected to increase. Savers will be less willing to forego spending and demand a higher rate of return so as to compensate them for the erosion of the purchasing power of money.

The supply of credit is not simply or solely determined by monetary policy. Over the short run, say during a year, the total amount of credit supplied by lenders, which includes individual savers, could increase by much more than monetary policy indicates. For example, in 1983 the net increase in outstanding credit, as measured by the Federal Reserve, was 29% larger than in 1982. This indicated a greater willingness on the part of lenders — individuals as well as institutions — to supply credit.

Credit that's used to build new real assets — producers' equipment, manufacturing plants and inventories — can and often does intensify inflationary pressures at a time when the economy, because of excessive income growth, is pushing against its capacity ceilings. When that happens, the bidding for resources is reflected not only in the higher interest rates as credit demands rise but also in the price for commodities and other real assets. But we are not now at that stage, and, even if we were, a single transaction such as the acquisition of the Gulf Oil Corporation by SOCAL wouldn't be critical because it is purely a financial transaction — cash which is a financial asset in exchange for another kind of financial asset — representing ownership of existing capital.

Credit used to acquire existing capital, as mentioned earlier, is a financial transaction, identical to the purchase and sale of common stocks, government securities and other debentures. To the extent borrowing is a new addition to the stock of credit, it flows through the market moving from owner to owner many times in financing the transfer of financial assets and, in the process, finances the building of new capital structures and equipment by those who sell new stock, notes and bonds into this huge fluid market.

Allocation of Credit

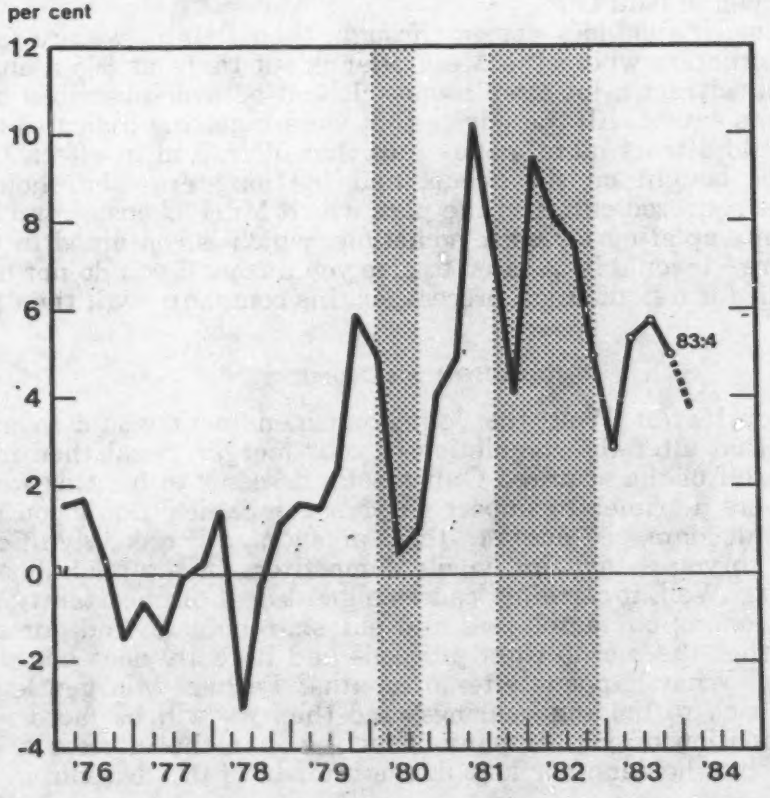
The marketplace allocates credit to the creditworthy — those with incomes that bespeak an ability to service and repay debt. Businesses with those capabilities have superior rates of return and so obtain credit more easily and more cheaply than those which are less profitable. Obviously, some strong borrowers become weak and some weak borrowers become strong over time as managements deteriorate or grow stronger. It is the efficient dissemination of information about risk among millions of borrowers and lenders that makes the market an efficient allocator of credit.

Individual borrowers have the advantage in today's highly competitive financial services industry of obtaining credit from a large number of competing suppliers. Brokerage firms, retail chains and credit card issuers have broadened their products to compete aggressively with such traditional lenders as commercial banks, savings banks and savings and loan associations. The gradual erosion of geographic barriers is enhancing the advantages of consumers as well as businesses in choosing among lenders. Business borrowers have also witnessed an explosion of credit instruments and the aggressive offerings of competing lenders. And for many borrowers, including the U.S. Treasury, investors living abroad have become aggressive buyers of U.S. financial assets.

Unlike prices for manufactured goods and services, interest rates — namely, the price for a service called credit — decline substantially in response to a decline in demand, which occurs when income growth slows down or when inflation abates and inflation expectations subside, making savers more willing to increase the supply of loanable funds. It is, in other words, a highly fluid market with many competitors and one in which what may seem to be a large transaction in absolute terms can and should be accommodated rather quickly without any disturbances in the marketplace. From the standpoint of the financial markets, the SOCAL acquisition of Gulf Oil Corporation is indeed a very legitimate exercise of the rights of capital ownership in our society, namely, to buy and sell.

In conclusion, a $13.2 billion transaction may seem very large in absolute terms, but when placed in the context of our extraordinarily large and efficient capital markets it can be accommodated quickly without any meaningful interest rate effect and without any deprivation to other borrowers. Indeed, the transaction provides a conduit by which funds will flow into the credit market to benefit other issuers of credit instruments, including the federal government.

Real 90-day CD rate



Shaded areas indicate recessions

The CHAIRMAN. Senator Hatch is going to have to leave in a few minutes for a hearing, so if there is no objection, I will call on him first for questions.

Senator HATCH. Well, thank you, Mr. Chairman.

I will only ask a few questions, but I think they are important ones.

Mr. Lee, had the Socal arrangement not been accepted, do you think Gulf could have continued to exist as an independent company?

Mr. LEE. Out of all the options we looked at, that appeared to us to be the only really viable one. We did consider a leveraged buyout proposal, which really was not an offer. That would, perhaps, have offered the best change of staying independent and maintaining the integrity of the whole system, but the money was not in place, and it was subject to getting the money, and we were told by the presenters that it would be March 21 before their money was available, and by that time, Mr. Pickens' offer would have been to the point where he could have bought at $65 a share.

Senator HATCH. Well, what do you regard as Gulf's options if the Socal deal falls through if this legislation is put through—what will happen to Gulf Oil?

Mr. LEE. If this does not go through, then I think we are faced with a situation where the Mesa offer is out there at $65 a share. That will attract a lot more money. It will be oversubscribed by a very large extent. All the advice that we are getting indicates that that would attract more money into that offer, and in effect, Gulf would be bought on the cheap, and the long-term shareholders would be squeezed out. And the plan which Mr. Pickens' group had been contemplating for quite sometime, which is contained in this book here—I would be pleased to give you a copy if you do not have it; it calls for a liquidation process for this company—will then proceed.

JOHNSTON AMENDMENT

Senator HATCH. Well, the Johnston amendment would seem to require that after the completion of your merger, Socal then must divest itself of the acquired Gulf assets. It seems to me this would be a severe detrimental impact on your companies. Don't you risk significant damage—doesn't this amendment risk significant damage to you as existing viable competitors in the oil industry?

Mr. LEE. Well, it certainly causes a great deal of uncertainty and anxiety among our employees and our shareholders, and our concern is that the moratorium proceeds and it really does not solve anything. What happens after 6 months? Perhaps you gentlemen will go back to holding hearings, and then we will be faced with the liquidation of our company. That is not in the interest of our 260,000 shareholders, nor is it in the interest of this Nation, in my opinion.

IMPACT ON GULF EMPLOYEES

Senator HATCH. Mr. Keller, there has been a good deal of discussion about the impact of the proposed merger on Gulf's employees and the communities in which they live. Should this merger be per-

mitted, and should the legislation that is proposed here not pass, what are you going to do about the impact on the employees of Gulf?

Mr. KELLER. Well, in the first place, both companies have in place a very favorable severence and retraining program. Certainly, in any of the alternatives, we are looking at some consolidation of operations.

As a practical matter, however—mention was made of Pittsburgh earlier—in Pennsylvania, we would hope that we could add the entire Gulf operation as far as the refinery, the marketing facilities, and so forth, to ours, because we are not a meaningful marketer, and we have no refinery in Pennsylvania.

The headquarters operation, which is relatively small, undoubtedly would to some extent be merged with ours and presumably, to some extent, disappear. I can make no unrealistic promises that a company can have two headquarters operations.

But I think overall, there is no question in my mind that the alternative that we have outlined is the one that will mean the most for the Gulf employees. The largest group of employees are involved in the exploration and producing end of the business, and this is the place where we feel that we have the greatest opportunity to take advantage of the talents, and the opportunities the leaseholds that the two companies have, working together.

IMPACT ON SHAREHOLDERS

Senator HATCH. Well, that is one of the greatest concerns I have, are the Gulf employees and the various shareholders in both companies.

In your testimony, Mr. Keller, you stated that every day of delay of the merger risks diminishing Gulf's value as a going concern. Could you just explain to us what the impacts of the delay on Gulf and on Socal's shareholders will be?

Mr. KELLER. Yes, I believe I can.

Certainly, the first one is a point which Mr. Lee mentioned—namely, in this area of uncertainty, if it stretches out for a matter of months, a great number of the outstanding Gulf employees, the ones that would have the easiest time finding competitive jobs in even today's market, would certainly be looking for such jobs, now knowing what lies in the future.

I think the financial strength which we bring to the business, and particularly the technological strength that the two companies have together, are the things which give us an importance to the national interest and to the search for energy.

Mr. LEE. If I might add just one word, please, sir, as far as the employees are concerned, I think one of the worst things about something like this is the uncertainty of it. It creates a tremendous amount of anxiety among our employees. And the sooner we know what we are going to do and how we are going to do it, the sooner we can deal with those uncertainties. This is what is bothering our employees so much right now, is the uncertainty of what is going to happen. And the sooner we can tell them, and deal with them on the certainty of the future, whether it is contingent employment

or whether it is separation with generous severance benefits, the better off our employees will be.

Senator HATCH. Well, I have a number of other questions that I would like to submit to you in the interest of time. I want to thank my distinguished colleague from Ohio for yielding to me for this purpose.

But let me just ask one last question of you, Mr. Keller, and that is this. My Senate colleagues have raised questions as to whether the new entity that will be formed as a result of this merger, assuming this legislation does not pass or is withdrawn, whether the new entity can afford to continue exploration and development work at the same pace as the predecessor companies did.

What would be the impact of your newly acquired debt on exploration programs?

Mr. KELLER. I think that is a very easy question to answer and one which has been horribly misrepresented by a number of the witnesses, I am afraid.

We borrowed money, or are in the process of borrowing it, in order to acquire a known thing, the known assets of Gulf Corp. Those assets in operation, as they will be very similar to the way they are now for Gulf, generate more income, including the investment program, than the cost of the funds.

So we are in a situation where we still have the entire Gulf program and the entire Socal program, coupled with efficiency, and certainly coupled with technological innovation.

I think there is just everything going for this, and I do not understand what this mystery is of borrowing money, somehow, therefore, raising your debt situation and restricting exploration. We do not borrow money for exploration. I do not know a banker in the United States who would loan me money for exploration. We borrow money to acquire assets that are measurable. But exploration, especially the frontier exploration we are talking about here, is a very high-risk business. We are looking at typical success ratios in the frontier of 1 in 15, or 1 in 20, with wells that cost $25 to $50 million apiece. This is an enormously complex business, and anything we can do to improve the stability of the companies doing it financially, and the quality of the human resources that are applied, is tremendously in the national interest.

Senator HATCH. Well, I will end with that. I know that there are arguments that you will not be as efficient, et cetera, et cetera. I suppose my colleagues will ask those questions, and I appreciate being able to ask the few that I have asked. This is really an interesting hearing.

Mr. KELLER. Senator, there is one point which has not really been brought up, which has a tremendous effect potentially on my shareholders. We have concentrated, I think quite properly, on Gulf. But legislation to halt this merger retroactively, particularly depending on the precise dates when legislation has been approved and when we have FTC clearance, could leave Socal and its shareholders in the position of owning all of the shares of Gulf Oil but maybe not owning anything.

Senator HATCH. And maybe having to liquidate at a loss after paying $80 a share.

Mr. KELLER. I think realistically that is the only practical conclusion.

Senator HATCH. One of the concerns I have is there are hundreds of thousands of little people out there who own shares in your companies, and that is what nobody seems to understand about the so-called big oil companies is that they are not single, monolithic entities. They are made up of just hundreds of thousands of individual shareholders, pension plans, mutual funds, and so forth. So it is not a simple issue. This is not some simple thing that you can just demagog. This is something that has to really be looked into. There are hundreds of thousands of people who will be affected if the right decisions are not made. And I have to admit, I have a lot of difficulty, when I understand the present antitrust laws and understand that they should take care of anticompetitive and monopolistic practices, which in my opinion are not here, and to interject a resolution or an amendment like this without answering all these problems of who gets hurt, and how, and when, and why, and whether it really benefits anybody, it seems to me is what is really worrying me right now.

I would say that in ending, and I apologize for taking as long as I did. I have a great many more questions for you, but I will just submit them to you in writing.

NUMBER OF STOCKHOLDERS

The CHAIRMAN. We will allow anyone to submit questions to the witnesses today, any member of the committee who wishes to.

Just a question or two, Mr. Lee and Mr. Keller.

How many stockholders do you have, approximately?

Mr. LEE. Approximately 260,000, sir.

The CHAIRMAN. Mr. Keller, how many do you have?

Mr. KELLER. Something over 300,000.

The CHAIRMAN. Well, that is about 550,000, or over half a million people, who would be affected if you merge.

Mr. KELLER. And maybe 400,000 if you allow for the overlap, yes, sir.

NEW EXPLORATION

The CHAIRMAN. Now I want to ask you both this one question. If this merger goes through as planned, will you do as much exploration by this new company as you both would have done had you not merged?

Mr. KELLER. I guess that is my question to answer, Senator, and the answer is definitely, yes.

The CHAIRMAN. The answer is yes, that you will do as much exploration?

Mr. KELLER. Yes, sir.

The CHAIRMAN. Will you produce as much oil if this merger goes through, by the new company, as both companies would have done if you had not merged?

Mr. KELLER. If I can answer that question—God willing, we will. Obviously, we are hoping to find some of that oil that we plan to produce, and I would like to think we can with great confidence assume that we can justify not only an accelerated exploration pro-

gram, but certainly, a very aggressive enhanced oil-recovery program, using the techniques that both companies have developed.

The CHAIRMAN. Now, Senator Hatch and I have another hearing we have got to go to, and I am going to ask Senator Specter if he will take charge of this hearing.

Senator, we are allowing each witness 5 minutes, and the Senators have not questioned these witnesses yet. You and Senator Metzenbaum and Senator Heflin are the three members of the committee present, but we have been allowing these other Senators to ask a few questions, too.

We will come back as soon as we can.

Senator Metzenbaum is next to question the witness.

[Whereupon, Senator Specter assumed the Chair.]

RETROACTIVE LEGISLATION

Senator METZENBAUM. Mr Keller and Mr. Lee, both of you have used the term that you do not think the legislation ought to be retroactive.

First, let me say that there was no question in the mind of anybody that this was a legislative issue that was coming back to Congress after it failed on a tabling motion the other day. It did not fail on its merits; it failed on a tabling motion. And Senator Johnston made it clear, I made it clear, and Senator Rudman made it clear that we were going to move forward at the next possible opportunity to enact legislation in this area.

So when you suggest it is retroactive, I think you were put on adequate notice. But having said that, let me say that it is not retroactive in any event. All you people have at the moment is a pending deal, and if we can enact legislation before you complete your deal, then our legislation in no way could be considered retroactive. Your deal has a way to go.

But I do not want to belabor that point. I want to get into some of what I consider the merits of this issue.

Mr. Keller, I tried to get up-to-date figures as of the end of 1983, but I could not. Can you tell me what stockholders 'equity was in Socal at the end of 1983?

Mr. KELLER. I do not have a specific number, Senator. I can certainly furnish that to you on Monday, if you like.

Senator METZENBAUM. Well, let's then go on the 1982 figures.

At the end of 1982, stockholders 'equity was $13 billion plus a little bit, and the total liabilities, current and longterm, were $10,244 million. Now, as I see that, the ratio of your assets to your liabilities at that point was 1.3 to 1.

Now, after the deal is completed, if my mathematics are correct, you will add to the liabilities of Socal $13 billion, and you will add Gulf's liabilities of $10.5 billion, for total liabilities of almost $34 billion.

Now, I may be wrong in my figures, and if I am, I want to be corrected. Gulf had liabilities at the end of 1982 of $10,522 million. So you would be picking up their liabilities; you would have $10 billion of your own liabilities, and you would have $13 billion of new liabilities.

Now, am I wrong in some respects?

Mr. KELLER. I am quite sure you are wrong, sir, but I am afraid that you are dealing with some numbers in a fashion which I won't try and answer here. I would be delighted to provide you with that information.

I think we are adding apples and oranges here to come up with these numbers.

Senator METZENBAUM. I want you to know, Mr. Keller, I do not add applies and oranges.

Mr. KELLER. OK.

Senator METZENBAUM. I understand financial sheets.

Now, I have here the Energy Daily which says, "What's more, taken on $12.5 billion of debt"—it is actually $13.2 billion—"would boost Socal's debt share from 7 percent of total capitalization at year-end 1982, the lowest among the majors, to 40 percent among the highest."

So that they come at it a different way as related to total capital.

Mr. KELLER. Yes; I can confirm those numbers, because they track exactly with those that I am familiar with.

Senator METZENBAUM. All right. Now, let me tell you that I am reading from the financial statements of Gulf and Socal.

Gulf at the end of 1982, as I read the figures, had equity shareholders of $9,914 million; had total liabilities of $10,522 million.

Now, you are certainly taking over their liabilities when you pay $13 billion to their shareholders. What really has happened in this deal is you are putting $13 billion out on the street—you are putting it to the shareholders, and the pension trusts, and whomsoever else holds it.

But as I see it, you would go from an asset value related debt of 1.3 to 1, to an asset value related to total debt of 0.67—in other words, 2 to 3.

Now, if that is the fact, it seems to me that any reasonable person would have to conclude that a company that was strong, and viable, and had a magnificent asset/debt ratio was putting itself into an asset/debt ratio far less desirable and far less able to provide the funds in order to go out and do the exploration.

Now, you have made the point: "When we go out to explore, we don't borrow money for that purpose." Of course you don't.

You have used the money that you have, the money that is available, either the money that you develop from profits or from depreciation or whatever the case may be. In your case, you are going to be saddled with payments of $1,300 million in interest—and how much additional will you be obligated to pay with respect to principal?

Mr. KELLER. Well, in the first 4 years, nothing. But nevertheless, we do plan a significant liquidation during the first 4 years. Particularly, we would anticipate—mostly because of Canadian Government regulations—the need to sell Gulf-Canada. This would reduce the debt about $2 billion.

I think the important thing here, Senator, is to recognize that we believe that we are receiving assets worth considerably more than the new debt that we are acquiring on a net basis.

Senator METZENBAUM. I understand that.

Mr. KELLER. We are also receiving earning capacity significantly greater than the cost of handling that debt.

Senator METZENBAUM. Tell me those figures. As I see it, Gulf in 1982 made $900 million—that is, I gather, after tax——

Mr. KELLER. Yes.

Senator METZENBAUM. I do not know what the pretax figures were.

Mr. KELLER. In fact, Gulf after tax, since we have to add back in both dividends and internal stock purchases, made $800 million more than that. After all, the Gulf dividends cease to exist, and these are after-tax dollars.

So we are looking at $1.7 billion of after-tax earnings, and of course, considerably more than that of cash flow, because of the depreciation of these assets. So there is significantly more cash generated and earnings generated, merely from the Gulf portion of the business.

Senator METZENBAUM. But you do not deny the fact that your assets-to-debt ratio is drastically changed in a Draconian manner, from having a positive value asset to debt, from 4 to 3, to 2 to 3?

Mr. KELLER. Senator, I will not disagree with you on those numbers. As I say, they are not numbers I am familiar with using.

I can say this, though. We anticipate using our own projections coupled with Gulf's, that at the end of 3 years, we would be back to an AAA credit rating. There are not many companies that can claim that.

Senator METZENBAUM. And what will you have at the time you conclude the deal—if that does become a fact, what will be your credit rating?

Mr. KELLER. It may be AA; it may be slightly below that. And, of course, the interest rates we are talking about are based on that assumption.

Senator METZENBAUM. And the interest rates you are talking about are about 2 points below prime?

Mr. KELLER. That is about right, yes, sir.

DOMESTIC RESERVES

Senator METZENBAUM. Mr. Keller, tell the committee what Socal's current domestic reserves are and what they will be if your acquisition of Gulf is allowed to go forward.

Mr. KELLER. Let's see. Oh, boy. These are numbers that ought to be sitting right in front of me.

We currently have in the United States about 1.3 billion barrels of reserves—in fact, I am sure you have those, because we have submitted the information, but they are numbers I choose not to remember sometimes——

Senator METZENBAUM. According to the figures we have here, you had 2,772 million barrels of oil worldwide proved reserves, and with Gulf, which has 2,919 million barrels proven reserves worldwide—does that sound correct to you?

Mr. KELLER. That sounds about right, Senator. Our U.S. figures, crude oil, condensate, and natural gas liquids, at the end of 1982, were 1.2 billion barrels for Socal—some 3.4 percent of the U.S. total—and Gulf's were 816 million barrels, or 2.3 percent of the total, giving the two companies when consolidated just a hair over 6 percent, between 6 and 7 percent.

Senator METZENBAUM. Well, Mr. Keller, would you explain to me how an acquisition which will substantially increase your reserves—more than double, as I understand, on a worldwide basis—how it is that you can relate to this committee that it will not diminish your need to find new reserves, and which at the same time significantly increases your debt and your debt-servicing expenses—isn't that bound to have some effect on your decisions as to whether to pursue risky new exploratory ventures?

Mr. KELLER. I do not see why it should. As I have tried to emphasize, Senator, these are two elements of the business which tend to be relatively independent of one another. Now, I will admit, if there were a dramatic drop in the price of oil, all of us in the industry would find it difficult to maintain some of the high-risk ventures. But we are making a very, very conservative assumption on oil prices; we are assuming they are at the same level in 1990 that they are today. And on that basis—and as I say, that is I think a very conservative assumption—on that basis, we can and will maintain an exploratory program of the same level that the two programs add up to today.

Senator METZENBAUM. But you had told me earlier in the day that you do not see the demand for oil rising in this country, or going all the way through, I think you said, to the year 2000. Am I correct about that?

Mr. KELLER. That is correct. I said we anticipate less than a 1 percent growth in that time.

Senator METZENBAUM. Therefore, you are going to have to give up, as I read this newspaper article, possibly 15,000 service stations. Is that a correct figure?

Mr. KELLER. I hope not. No; I did not write the newspaper article, Senator.

No; we would envision that the number of service stations we acquire from Gulf will be very much a function of what we can negotiate with the Federal Trade Commission. I would hope that the great bulk of the outlets which Gulf currently has can be consolidated with our own.

Now, there are some areas where, based on what we have seen as recent positions taken by the FTC, that we would have to reduce and sell to one of the many companies which have been pursuing us in the last week, some of those operations.

NUMBER OF FILLING STATIONS

Senator METZENBAUM. How many stations do you have?

Mr. KELLER. Well, owned and controlled, we have about 4,000. We have a great many jobbers which we supply, and in addition, many independent dealers which we supply.

Senator METZENBAUM. And they sell Standard Oil?

Mr. KELLER. Only the branded jobbers. The others sell products under their own names, the many different names you see up and down the street.

Senator METZENBAUM. And Gulf?

Mr. KELLER. Gulf has—I believe I should leave that to Jim.

Mr. LEE. About 15,000 in total, sir. And that, again, is the total of all the dealer-owned, company-owned, and jobber-owned stations.

Senator METZENBAUM. Without prejudicing your position with the FTC or the Antitrust Division of the Department of Justice, isn't it reasonable to assume that you will be forced to give up a substantial number of your marketing facilities, particularly in those areas where you and Gulf presently both have operations, and as a consequence of that, is it not the fact that your opportunity to market your product is going to be decreased; your reserves will be up, more than double what they are at the moment, and the real incentive to go out and find additional oil will not be there, because you will have more than enough to begin with?

Mr. KELLER. Well, there are two points there where I have to disagree with you, Senator. In the first place, I would hope that the Federal Trade Commission would see as the most competitive posture for our company one in which we retain nearly all of the Gulf outlets. There are only five States—they are all in the Southeast—in which the two of us have significant shares, and I would assume that we would have to make some special arrangement in those five States.

I think there is an unfortunate theory that seems to pass around when people talk about the industry, that there is some relation between our crude-oil production and our crude-oil marketing. These are almost completely unrelated ends of the business. Crude oil today is a fungible commodity in trade. We sell most of our crude to people other than ourselves, and we buy most of our crude from third parties. And I am sure exactly the same thing is true for Gulf. This is the very nature of the business. What we have here is not a tie between the wellhead and the gasoline pump.

Mr. LEE. If I might say so, sir, on that point, one of the reasons that we came back to the United States for so much of our investment, which we have done in the last few years, is the fact that you do not have to find a market for the crude oil. We are short of crude oil in the United States, and we are still importing several million barrels a day; whereas, if we were finding oil in the Middle East or somewhere else, we would have to in effect bump heads with the OPEC marketers and shove our way into that market. In the United States, the market is already here, and that is one of the reasons that we have really come back and put the bulk of our exploration money back into this country, plus the fact that the stock market here values the reserves in this country so much greater than it values them outside the United States.

Senator METZENBAUM. Mr. Keller, you made the point that the interest that you will be paying out will be taxable and that it is taxable to the recipient. I think you made that point——

Mr. KELLER. In general, yes, sir.

LOANS FROM BANKS

Senator METZENBAUM. All right.

Mr. Keller, do you serve on any bank boards?

Mr. KELLER. Yes, sir.

Senator METZENBAUM. Which one, may I ask?

Mr. KELLER. First Interstate Bank.

Senator METZENBAUM. And that is located where?

Mr. KELLER. In California—well, it operates in 11 States. First Interstate Bank Corp. and First Interstate Bank of California.

Senator METZENBAUM. Do you know the effective tax rate of that bank?

Mr. KELLER. The bank itself has a relatively low tax rate, yes, sir. But that is not really the source of a good part of this money, either. It is not owned by the banks. It is coming from all elements of the financial community. And we would expect that a good part of this debt will be converted into term debt, which will be much more widely held.

Senator METZENBAUM. Into what?

Mr. KELLER. Into term debt; 4- to 8-year, probably, or maybe even longer.

Senator METZENBAUM. If it is not coming from banks, where is it coming from?

Mr. KELLER. You and me, among other people, I guess. Bonds are very widely held, I am sure you will agree, Senator.

Senator METZENBAUM. The $13 billion, I am talking about.

Mr. KELLER. Initially, it is coming from banks; yes, sir.

Senator METZENBAUM. Initially, it is coming from banks.

Mr. KELLER. No question.

Senator METZENBAUM. And you are aware of the fact that in spite of the fact that Congress goes way out of its way to see to it that oil companies get the finest tax breaks of almost any industry in the country, you still run behind the banks as far as paying low tax rates. The 20 biggest companies, I think, last year paid something like 2 percent. So that, although you say this interest income is taxable, as a matter of fact, it goes to banks, and there is very little likelihood that any of it or much of it will redound to the Federal Treasury.

Mr. KELLER. I appreciate that.

Senator METZENBAUM. All right. I have some additional questions, but I told the chairman that I thought we ought to rotate, and I may want to come back. But I will yield.

Senator SPECTER. Thank you, Senator Metzenbaum.

Mr. Keller, picking up on one of the points that Senator Metzenbaum asked you about, will you agree that if legislation is passed at some date in the future, affecting the Gulf/Socal merger that it would not be retroactive?

Mr. KELLER. I am not quite sure what you mean by the question, Senator.

Senator SPECTER. Well, the question means would it apply to you after the fact, after something you have done.

Senator Metzenbaum was developing a point that the legislation would not be retroactive, and I thought you might want to have a leading question the other way. [Laughter.]

Mr. KELLER. I do appreciate that, Senator. I am sorry I did not pick up just a little sooner.

At any time there is an enormous amount of legislation pending in this House and in the House on the other side of the Capitol, and certainly, we try to keep abreast of legislation which is in process. The mere fact that another piece is introduced on a particular evening as a supplement to an unrelated bill and with no hearings

is hardly what I would call putting one on notice that this is a likely piece of legislation.

Senator SPECTER. Well, for good or ill, you were very far down the road before you had any notice that Senator Johnston, or Senator Rudman, or anybody else was going to introduce legislation which would hold up the merger efforts.

Mr. KELLER. Well, we were in terms of our preparing to respond to Mr. Lee's invitation, and obviously, in terms of our appraisal of the offer. And certainly, Mr. Lee was much further down the road.

Senator SPECTER. Well, Mr. Lee, let me ask you a few questions about the impact on Gulf jobs. I am sorry that I was not here before, you may have covered some of this. But what estimate do you have concerning how many Gulf jobs will be lost through the merger with Socal?

Mr. LEE. We do not have that number yet. That still has to be developed.

NUMBER OF EMPLOYEES

Senator SPECTER. What is the total number of people employed by Gulf?

Mr. LEE. It is approximately 42,000 worldwide; in the United States, about 27,000.

Senator SPECTER. And how many of those 27,000 are employed in Pennsylvania?

Mr. LEE. I am sorry, I lost you.

Senator SPECTER. How many of the 27,000 employed by Gulf in the United States are employed in Pennsylvania—I will not ask you for any other State.

Mr. LEE. I am sorry. I will have to get you that number. I should have had it, and I do not have it.

Mr. KELLER. May I comment on that, Senator, not in terms of numbers, but in terms of roles. I am sure the largest number of those employees are involved in refining and marketing, particularly at the Philadelphia refinery, and it would not be our intention to make any dramatic changes, except as required by the Federal Trade Commission, with regard to the refining and marketing operations in Pennsylvania.

The headquarters situation certainly is somewhat different, and I really cannot tell what would happen there.

Mr. LEE. Excuse me. I would say there are approximately 2,000, but we will get you the exact number.

Senator SPECTER. About 2,000 in Pennsylvania.

Mr. LEE. Approximately; yes, sir.

Senator SPECTER. And how many are employed, Mr. Lee, in the headquarters operation in Pittsburgh?

Mr. LEE. Approximately 700 now.

Senator SPECTER. I had seen a figure of 900; is that a good figure?

Mr. LEE. I cannot quite reconcile with the 900, but I think it is somewhere around 700.

Senator SPECTER. Would you expect most of those jobs to be lost as a result of the merger?

Mr. LEE. Well, that depends on Mr. Keller and Socal, really.

Senator SPECTER. How about it, Mr. Keller?

Mr. KELLER. I do not know that most of them would be lost, but I would be surprised if they stayed as a headquarters operation. There are certainly a great number of people in that organization who could play a significant role in our own. Now, I appreciate that does not retain, necessarily, citizens employed in Pittsburgh in the headquarters, but more likely, employed administratively and in other roles within the joint company.

Senator SPECTER. Well, are you saying that some jobs will be lost in Pittsburgh, but you will make an effort to relocate as many people as you can?

Mr. KELLER. Yes, sir; that is exactly right. You put some very satisfactory words in my mouth, I think. We certainly will use every effort to relocate, retrain, and we have a commitment pretty well spelled out with regard to termination settlements and severance arrangements for those who would leave.

Senator SPECTER. But notwithstanding your efforts, at least 700 jobs will be significantly at risk in the Pittsburgh area?

Mr. KELLER. I think that is a fair statement, Senator.

Senator SPECTER. How about in the balance of the State, Mr. Lee? Mr. Keller has testified that the refinery would be retained in the Philadelphia area. Would you expect other jobs to be significantly at risk in the balance of Pennsylvania?

Mr. LEE. Again, I think that is Mr. Keller's decision and his people. From what he has said, he would hope to retain most of the assets or all of the assets in the refining and marketing system there, and that is where most of those other employees are involved.

Senator SPECTER. You would expect, aside from the headquarters, not to have a significant number of jobs at risk; is that a fair statement?

Mr. KELLER. That is right. We are not a significant marketer in Pennsylvania, as you probably know, Senator, so we would need these people in order to maintain those operations.

Senator SPECTER. When you say "not a significant marketer in Pennsylvania," to what extent does Socal, Chevron, have operations, stations, in Pennsylvania?

Mr. KELLER. Well, we have no refineries that are operating on the east coast now. We did have one at Perth-Amboy refinery, which is just an asphalt refinery, and we operate from there into the eastern part of Pennsylvania. But as I recall, we are a 2 or 3 percent marketer in that market, not a very significant presence.

Senator SPECTER. So, how many service stations would you expect to be closed as a result of——

Mr. KELLER. I see no need necessarily for any to be closed. Now, we have not had the opportunity, of course, to lay out our precise arrangements. Certainly, if we had stations nextdoor to each other, obviously, things would have to be arranged, and we would make these available in the market.

Senator SPECTER. Well, I would appreciate it if you would provide the committee with a response on that issue, as to what would be closed by way of Gulf or Chevron stations, assuming the merger goes through. Also, as precise a figure as you can about jobs that are at risk in Pennsylvania as a result.

Mr. KELLER. Senator, I will do the best I can. Of course, with the limited information we have, it may be a range. But we will do our best to provide that to you promptly.

Senator SPECTER. All right; I would appreciate that.

Mr. Lee, I think it is important to put on the record at least briefly the considerations that led Gulf to choose to deal with Socal as opposed to the Mesa operation. Perhaps you covered that before, or have you?

Mr. LEE. I covered a little bit in my written statement. I did not develop it very deeply, though.

Senator SPECTER. Well, would you, please? Why does Gulf prefer to do business with Socal, as opposed to Mesa?

Mr. LEE. Well, there are two different situations, entirely. Our reading of the intentions of the Mesa group if they took over would be to liquidate this company, either in part or in whole. This does away with the exploration effort, it does away with the employees' jobs, if not immediately, certainly in a matter of a few years. In fact, the plan in this book that I referred to earlier calls for liquidation by the end of 1986, whereas in the case of Socal, they are proposing to continue the operations—certainly, most of our employees will continue with jobs. And I think just as important, also, from the standpoint of our shareholders, the cash offer for all of the shares at $80 a share is significantly better than they would fare at the $65 tender offer out of Mesa.

Senator SPECTER. Mr. Lee, this is something that you and I had discussed in part before, but for the record, what arrangements, if any, have been made for you and the other officers as contrasted with other employees?

Mr. LEE. We have no employment contracts in our company. The three senior people said we did not want contracts. When we were in our proxy fight, we told the shareholders that we called on that we had no golden parachutes; we had no contracts, we did not intend to ask for them. And that is still the situation. If we are severed, all we want is what is coming to us in the way of normal retirement benefits and the value of our stock and that kind of thing.

We did give 17 people contracts, mostly short-term people who would have really suffered from the standpoint of not having built up any pension benefits of any considerable amount, and those were all more junior people—certainly, not as senior as the three top people.

But there are no contracts for any of us, particularly us in the executive and senior management.

Senator SPECTER. Mr. Lee, what would happen to Gulf in your judgment if the merger is stopped by Senator Johnston's legislation?

Mr. LEE. Well, it depends on what happens at the end of 6 months. It is going to be a very, very difficult situation for us if we are left in limbo, in effect, not knowing what is going to happen on down the road. That is the worst of all worlds, as far as we are concerned. I think it is the worst situation for our shareholders and our employees. We already have a lot of concern and anxiety among the employees. I am concerned already about losing some of our very valuable people. The headhunters are out, and they are asking our people for résumés. I am concerned about keeping them

with us now. With this additional uncertainty that would be created if indeed you went ahead with this proposed legislation, I think it would make it very, very difficult for us to function in any kind of normal way over the next 6 months.

Senator SPECTER. Just one question for you, Mr. Keller, and then I will pass on to Senator Johnston. Assuming the merger between Gulf and Socal is obtained, what is the then potential threat to the newly merged company as a target for takeover?

Mr. KELLER. I assume the potential does exist. We certainly would anticipate that the strength of the company would put us in a far better position than either of us would be alone. Our shares, I must admit, are far undervalued. Shares in the industry today are valued based on current earnings, not on asset value. I guess a fair analogy would be a real first-class hotel in a community that has very few visitors. You have a valuable asset, but there is not enough business to make it a very attractive investment, and if you wanted to sell it, the sales price would relate most likely to what it would earn, and that is what happens on the stock market.

Senator SPECTER. Mr. Keller, if the Gulf/Socal merger were exempted, would you oppose Senator Johnston's proposed 6-month moratorium?

Mr. KELLER. I think on principle, I would have to, Senator. I do believe that it is a mistake to pick an isolated industry, one which is highly competitive, and arbitrarily say, "Stop for 6 months." In the first place, I think I would have to say I am skeptical about 6 months. That leaves us just before the election, and I think most of you gentlemen would have other things that were occupying your time.

Secondarily, I think it would be very healthy if there were substantial hearings promptly on the matters at hand. I think it would be appropriate for the various committees to take a look at whether predatory takeovers are in the national interest—and ours with Gulf is certainly not predatory, though I must say, a predatory attempt precipitated it—and what is it that should be done that would not be a case of trying to solve, perhaps, a nonproblem with a sledge hammer. I think we need at least to consider what sort of legislation would be in the national interest and still maintain a real free market for those who trade in our securities markets and for those who try and conduct our national businesses.

Senator SPECTER. Senator Johnston.

Senator JOHNSTON. Thank you, Mr. Chairman.

Mr. Lee, I want to congratulate you on your choice of a white knight. I think you picked a good company with a good chairman, and if anybody can make a good deal of it, Socal can.

I know, Mr. Lee, that you were aware of the problems of the undervaluation of Gulf's stock and were engaged in an ongoing program to put Gulf back on its feet. I think you fired some 14,000 employees in order to get lean and mean; is that about right?

Mr. LEE. Well, we are probably about 13,000 or 14,000 less than we were a couple years ago. Not all of them were fired. Some of them went with vested businesses.

Senator JOHNSTON. Right. But in other words, you had an ongoing program to put Gulf back in a better dividend situation to get the value of the stock up?

Mr. LEE. Yes, sir.

Senator JOHNSTON. Had you been given time, do you think you could have done that in the interest of the stockholders?

Mr. LEE. Well, we have made a lot of progress, and we think we would have made a lot more, yes. I think we could have, over a period of time, gotten our stock price up, certainly, from where it was, and moved it on up. That was our intention. And I believe we were making good progress, and we had every reason to believe that we would continue to make progress in that respect.

Senator JOHNSTON. All right.

You resisted the attempts of Mr. Pickens because you really believed that you could operate that company in the interest of the stockholders, and of the country, indeed, better than he could in liquidating the company; did you not?

Mr. LEE. Yes; we resisted the efforts—particularly, we fought over the royalty trust in our proxy fight, and our concern there was that the individual shareholders were disadvantaged compared to the corporate shareholders, plus the fact that it really would be a liquidation strategy, and that was the furthest thing from our mind.

Senator JOHNSTON. Now, with a company with almost $3 billion in reserves—and how much cash flow did you have?

Mr. LEE. Roughly $3 billion.

Senator JOHNSTON. A company of that size, you did not feel like it was too small, back, let's say before the Pickens takeover; you thought it was adequate to drill on the Outer Continental Shelf; I think you were in the nuclear business, and I think you were in some other energy businesses, I think maybe even the coal business. You thought the company was adequate in size at that time, didn't you?

Mr. LEE. Yes, sir; I would say so.

Senator JOHNSTON. And before the Pickens attempt, you had not been out, looking for white knights, even as likable and as capable as Mr. Keller is; you thought you could do very well with Gulf on its own, located in Pittsburgh, as you were, with your program ongoing—didn't you feel that way?

Mr. LEE. I felt like we were making very good progress; yes, sir.

Senator JOHNSTON. And so, the attempt to get Socal and Mr. Keller and your white knight was brought on solely because of what has been described as a predatory takeover attempt by the Pickens group; isn't that correct?

Mr. LEE. That is correct, sir.

Senator JOHNSTON. And isn't it also a fact that you would still be here today, testifying that Gulf can better be operated by Jim Lee and company, in Pittsburgh, PA, as Gulf Oil, but if you never had had that takeover attempt, you would be here defending Gulf Oil, its integrity, its efficiency, its long-term plans, its place in the market, were it not for the predatory attempt to take your company over.

Mr. LEE. Yes, sir. We were faced with an actual tender offer at $65 a share, and we had to respond to that.

Senator JOHNSTON. Right. Now, if that is so, I think it also follows that you do not think that predatory attempt was in the na-

tional interest, and certainly not in the interest of Gulf or Gulf's shareholders, do you?

Mr. LEE. I do not believe it was; no, sir.

Senator JOHNSTON. Well, shouldn't we do something about that?

Mr. LEE. I think if you did, you would be addressing the real problem. I do not think the real problem here is the merger of Gulf and Socal. I think that is the result of the problem that you are speaking of.

MERGERMANIA

Senator JOHNSTON. And am I wrong when I say that this, what I have described as a hurricane, or a whirlwind, or a mergermania, that is now $29 billion pending, that it is likely to sweep companies like PhillipSun, Amarada-Hess, Union-Cal, Kerr-McGee, Texas Eastern, et cetera? Am I wrong to think that the same thing that happened to you may happen to them?

Mr. LEE. I would think it could, and I think that some of them think it could, too.

Senator JOHNSTON. And if we have 29 billion dollars' worth of these deals hanging fire now, and at least in your case, the attempt by the Pickens group was not in the national interest, not in your stockholders' interest, not in anybody's interest, and we have got all these others, which add up to $50 billion to $100 billion, that means that we really ought to do something about it. I guess I am asking the same question over again, and I guess the answer is yes again.

Mr. LEE. I think if you did, sir, you would be getting to the root of the problem.

Senator JOHNSTON. Now, a moment ago, we talked about the retroactive effect, and I just want to get one thing clear. This deal is not done yet; the shares are not purchased, either the Pickens shares or the Socal shares, and indeed, as I understand it, we referred to a "binding contract." Just for the record, doesn't that so-called binding contract have a force majeure clause which specifically references congressional action? Is that right, Mr. Keller?

Mr. KELLER. It is, with one limitation that we must recognize. It is a binding contract with FTC approval. At that point, we must acquire the Gulf shares. In other words, the force majeure would have to occur before that to be meaningful.

Senator SPECTER. And wouldn't you guess that would be sometime in mid or late April?

Mr. KELLER. I would guess it would be within, yes, a month or so.

Senator JOHNSTON. And, knowing the way the FTC works, if, for example, the Senate had acted on this, and had ruled to exclude it, I would not think they would rush to judgment on approving the matter.

Mr. KELLER. I am not familiar with the FTC's procedures, Senator. I should not comment on that.

Senator JOHNSTON. Well, like the Supreme Court, I think they read the election returns and the acts of Congress.

Now, Mr. Lee, if we can prevent this by this legislation, if we can put you back in the status quo ante—and I am not asking you to

say whether we can or not—but if we could do that, restore the old Gulf, isn't that in the national interest?

Mr. LEE. I wish—yes; I think it probably could be, if you could make it happen. I have a little trouble understanding how you can unring the bell on all these events that have transpired, sir.

Senator JOHNSTON. Well, we think we have a way to do that. But let's say that we do not, that we stop the deal for 6 months, Congress looks at it and says, "Jim Lee is wrong. Predatory acquisitions are not predatory at all. That is the invisible hand working, that is inducing efficiency into the market," and all those things. Then, this will not be the last offer you have got. You and George Keller will still be friends; you will still think he is a good white knight. He will still have greater purchasing power, less debt equity ratio than anybody there is, and you can probably still make this deal again, can't you?

Mr. LEE. I do not know. That would be up to Mr. Keller. At that point, I would think I would probably be begging him to. I must say, though——

Senator JOHNSTON. I think he is a good guy, and he would say yes.

Mr. LEE. My concern is that if it did not happen that way, then you would have discriminated, really, sir, against 259,955 shareholders of Gulf.

Senator JOHNSTON. We do not want to do that. We want to put Jim Lee back where he says he ought to be.

One final thing. Mr. Keller, there is a word they call shark repellent. I am sure you know what that is. Does Socal have adequate shark repellent after this deal or are you going to be looking over your shoulders, about three rows back, for a shark?

Mr. KELLER. We have no formal element of shark repellent—that probably is not something I should say out loud in a public forum. On the other hand——

Senator JOHNSTON. Your stock may go up tomorrow.

Mr. KELLER. That is a nice thought. I can assure you, it bears no relation to the asset value.

We do not have any shark repellent devices. We reviewed with the board about a month ago that possibility and concluded that we really did not think they were appropriate, that we would stand on our own strength and see if we could not handle that kind of problem if it arose. Certainly, we would be in many ways stronger, I think, to resist such an attack after this merger. But that is really a separate question.

A lot will depend on what, if any, legislation might materialize in various areas within this house.

Senator JOHNSTON. I hope you will speak to Mr. Lee about what is adequate shark repellent, what works and what does not.

Mr. LEE. I can tell him a lot, sir.

Senator JOHNSTON. Thank you, Mr. Chairman.

Senator SPECTER. Thank you very much, Senator Johnston.

Senator Nickles.

Senator NICKLES. Thank you, Mr. Chairman. I will try and be brief.

Mr. Lee, my good friend and colleague, Senator Johnston, led you through a nice little scenario, in which you said you felt like

maybe there need to be some changes. For the record, are you for or against this legislation?

Mr. LEE. Against the legislation, sir, as I understand it.

Senator NICKLES. OK. Are you against the legislation if it would just be effective on date of enactment and not go all the way back to February 28?

Mr. LEE. I do not think I could argue with it at that point.

Senator NICKLES. So you would not be opposed to the legislation if it were made effective on date of enactment?

Mr. LEE. Well, let me say this. I think a moratorium in itself really does not address the issue. The moratorium just leaves everything hanging, and that is my concern with the legislation, as I understand it right now. It is what happens after the moratorium that really becomes so important. But certainly, from a retroactivity standpoint, again, just for the record, I certainly do not believe that we had any information on what was really being proposed. We had some information that there was a bill, but I think it was quite somewhat different from the one you are looking at now, but we made our decision to go and find somebody on February 24, and I think that was before the date here that was talked about for the bill.

But the bill itself, I think, does not really address the real problem.

Senator NICKLES. Let me make this real clear, then, because I think it is important, and Mr. Keller has already answered this question, but I want to find out exactly where you stand.

You are opposed to the legislation as it is right now, and right now it is retroactive and would basically void the Socal-Gulf deal, or at least it would postpone it for 6 months, and we would then have to see what would happen?

Mr. LEE. Yes.

Senator NICKLES. Now, many people are considering different alternatives, one of which is just to make the legislation prospective, and whatever deals have been entered into prior to date of enactment would be allowed to go through, that is, similar to the Texaco/Getty situation.

Would you support or oppose this legislation if it was prospective?

Mr. LEE. Well, I think I would take advice from counsel on that one before I really made up my mind, but again, I have a lot of heartburn with the legislation as it is proposed, whether it is prospective or retroactive, and I think I stated that already.

Senator NICKLES. Some of us have heartburn with the legislation not just in dealing with the Socal-Gulf deal, but also the cloud that it would hang on the entire oil industry. Do you think that is a problem?

Mr. LEE. That is one of the things I am talking about.

Senator NICKLES. Let me ask you another question. You mentioned that you did not really feel like this legislation would get to the root of the problem. Senator Johnston, I think, and Senator Metzenbaum are looking for a 6-month period of time to establish a commission to look at the problem. Since you see this legislation as not being the solution and several Senators mentioned proposals

that might basically restrict mergers through tax law changes, do you think that is a direction in which we should head?

Mr. LEE. I really do not know which direction you should go, Senator. I just think that this bill as we see it certainly does not begin to really deal with all of the issues. It creates much more uncertainty and anxiety. It leaves us in limbo, certainly. And I think if you want to get at this whole matter of mergers and the reasons they are happening, then I think you need a lot more studies and hearings on this.

Senator NICKLES. Well, you have had some time. I think Mr. Keller addressed one of the reasons why so many of them are happening, and that is because the assets are very large and the earnings, and therefore, the prices are very low in comparisons to the assets.

Now, Mr. Keller, I would think if I were in your chair or if I were in a comparable company's chair, I would be trying to manage the company in a way that would increase the dividends that would be paid, and therefore increase the price in relation to the assets, so you would not have a cheap, easy takeover.

Mr. KELLER. That is certainly one of the top objectives, but we have come here upon one of the very significant differences between Wall Street and a business like ours. Unfortunately, and to a large extent I think because of the way the tax laws function for various groups, Wall Street tends to have a very short-term evaluation of performance. There is no way you can run a major oil company on a short-term basis. We are looking at events, particularly as we are involved in major exploratory and development projects, activities that run 8 or 10 years, and when we start talking synthetic fuels or complete new concepts, we are talking much longer than that. And as a result, the very nature of the business is one involving a high reinvestment, a high series of risks, only some of which prove successful; and as a result, in an environment like today's, a relatively low ability to earn based on the value of the assets.

Senator NICKLES. Just a couple questions. You have a binding contract now between the two companies; is that correct?

Mr. KELLER. Yes; we do. We have a merger agreement and have a tender offer outstanding to the shareholders of Gulf, which becomes a binding contract when we clear the Federal Trade Commission requirements.

Senator NICKLES. If this legislation were to pass, and during this 6-month period of time, the FTC said there was no problem, are you at cross-circles—are you compelled by your contract to purchase the stock, and then by this legislation told it is unlawful for you to acquire control?

Mr. KELLER. May I ask my director and vice president, Legal, Judge Renfrew, to answer that? I do not feel comfortable with the legal complications.

Mr. RENFREW. Excuse me, Senator. Under the contract, if the approval comes before the enactment of the legislation, we would be obligated to acquire the shares and complete the tender offer. If, however, the legislation is enacted before that date, we of course have a clause in our contract which precludes us from having to conclude the transaction.

So it all depends upon the enactment date of the legislation.

Senator NICKLES. Asking Mr. Lee, then, the counterpart of that question, let's say the legislation went into effect before the approval went through and before the shares were acquired. Then, what would be your relationship with Mesa, which has already acquired a certain percentage—what would that be, 13 percent, today——

Mr. LEE. That is about 13 percent, correct.

Senator NICKLES [continuing]. Tendered an offer that would take it up to 22 percent.

Mr. LEE. Yes, sir.

Senator NICKLES. This would foreclose the additional acquisition during this period of time. I do not know—the Senator might be able to tell me—would it force Mesa to sell the stock that is above 5 percent at the conclusion of the 6 months?

Senator JOHNSTON. If there were no legislation enacted?

Senator NICKLES. Yes.

Senator JOHNSTON. If Mesa, on its tender offer, acquires additional shares exceeding 5 percent of the value of Gulf——

Senator NICKLES. They already have 13.

Senator JOHNSTON. Yes, they would not be required to divest the 13, but they would be, any additional shares that exceeded 5 percent that they received after February 28.

Senator NICKLES. OK. And Mr. Lee, if this did happen, under this scenario, would Mesa have effective control with as little as 13 percent?

Mr. LEE. Not by themselves, but——

Senator NICKLES. Through a proxy?

Mr. LEE. Given where we are now in the marketplace, I think all the advice we are getting is that if we went ahead with a shareholders meeting and got into a proxy fight, that the odds were that the Mesa group would indeed be able to elect the board of directors of our company.

Senator JOHNSTON. Would the Senator yield at that point?

Senator NICKLES. Certainly.

Senator JOHNSTON. The legislation does prohibit the solicitation of any proxy consent or authorization with respect to voting of securities, so it would outlaw the proxy fight.

Senator NICKLES. So with 13 percent without additional proxies, would there be effective control?

Mr. LEE. I would not think so—I do not know—Counsel, have you got any advice?

I do not think so, sir, unless we were actually in a proxy fight per se.

Mr. RENFREW. Senator, there is one point. The legislation changes daily, and so I do not have before me the most recent version, so it is very difficult to address legislation in a state of flux.

However, the last version that I saw yesterday had a provision which did restrict anyone who had an interest in a royalty trust from acquiring any shares in one of these 50 largest oil companies.

My understanding is—and of course, we have a witness who can tell us about it—that the royalty trusts have been transferred from Mesa to another corporation, Mesa Royalty or some type of name like that, and that Mesa itself does not have any royalty trust. So it is not precluded from making an offer or acquiring shares in

Gulf at the present time, and the facts are such—and they are so complicated, it is very difficult to deal with legislation trying to prohibit a specific person from taking certain acts in a free enterprise system.

Senator NICKLES. Thank you.

Senator JOHNSTON. If the Senator would yield, we have that covered; that has been added. [Laughter.]

Mr. KELLER. Senator, may I raise one further question, though, and I think really, the basic one——

Senator SPECTER. Mr. Keller, would you do so briefly, because we have a long list of witnesses, and we want to move ahead.

Mr. KELLER. Yes, Senator. It is really this. The expectations of the current shareholders of Gulf are for a sizable sale price. If the regular proxy arrangement, the regular election of directors of Gulf were to come up today, I have very little doubt, and I think Mr. Lee has confirmed his view, that a board other than the present board would probably be elected, and would probably dissolve the company.

Senator METZENBAUM. Well, I think it is fair to say that if the amendment as presently drafted does not resolve the problem of putting a halt both to the Socal-Gulf merger as well as the Mesa takeover, then I think it just relates to our ingenuous in figuring out a way to do it, because it is the intent of the sponsors of that amendment to do just that, and I believe that where we have that intent, provided we have the votes, that we can do it.

Mr. KELLER. Senator, I hope you do not do it by disenfranchising either Mr. Lee's shareholders or mine. I think that is really where you would comeout.

Senator METZENBAUM. We will not do that.

Senator JOHNSTON. We will not do that.

Senator METZENBAUM. We might do it through the tax laws, as Senator Specter has suggested, or some other ideas that some of us have explored with the Finance Committee.

Senator SPECTER. Mr. Keller, you and Mr. Lee could give us some assistance on this. We are dealing with extraordinarily complex matters, and we are searching for alternatives to be as ingenuous as those who are out after predatory takeovers. And when you gentlemen came to see me earlier this week, I raised these issues with you. As many people as we have back here, we have limited staffs. And I am recently from the legal profession and know the kinds of talent which are brought to bear for the corporate interests on matters of this sort. And we can use assistance of a technical nature to figure out ways to accomplish the objectives which we have been very plain about.

Mr. KELLER. Thank you, Senator. We would certainly be glad to work with you. I think we have two questions, though. One is how do you put Humpty-Dumpty back together again—which I do not think we can conceive of—the other is what might be done to reduce the risk or the incentive for predatory takeovers, and we would certainly like to work with you on that.

Senator SPECTER. Well, you're facing two situations. One situation is whether Gulf can be restored without Socal, and the other is whether predatory takeovers can be stopped in the future.

I have an instinct that if the Congress can find an answer to question 2—how to stop predatory takeovers in the future—that the Congress would be very happy to settle on that, and that reconstructing, issue 1, how to put Gulf back together again, is a lot tougher question and involves a whole lot of equities which have already come into play. You start talking about dates, you start talking about a lot of technicalities, and we understand the equities which are involved.

Well, gentlemen, thank you very much. I believe that concludes the questions which we have for this panel, and we will be in touch further.

Mr. LEE. Thank you, Senator.

Mr. KELLER. Thank you.

[The following was subsequently supplied for the record:]

QUESTION #1 In response to Senator Specter's question on lines 1 through 6 on page 142 of the transcript.

"Senator Specter asked me how many service stations in Pennsylvania I would expect to be closed as a result of the merger. I replied that I did not see any necessity for any to be closed. I commented that we had not had an opportunity to make specific plans, but that if Gulf and Socal owned stations next door to each other, it is possible that one station or the other might have to be sold. Senator Specter asked me to review this matter further and provide the Committee with as precise a figure as possible about the number of Gulf or Chevron stations that would be closed and the number of jobs that are at risk in Pennsylvania as a result."

After reviewing the matter, I believe I was correct when I said there probably would be no need for any Gulf or Chevron service station in Pennsylvania to be closed.

Socal does not now own any service stations in Pennsylvania. We supply gasoline to 15 Chevron branded jobbers, i.e., distributors, who do business in Pennsylvania. Those jobbers supply Chevron gasolines to about 210 Chevron branded service stations in Pennsylvania. These service stations are either owned by the jobber or by third parties.

Gulf's marketing operations in Pennsylvania are much more extensive than Socal's. We understand that Gulf owns about 130 service stations in Pennsylvania and directly supplies about 225 Gulf branded stations which are owned by others. In addition, Gulf supplies about 35 Gulf branded jobbers in Pennsylvania who in turn supply approximately 600 additional Gulf branded stations.

Because Socal owns no stations in Pennsylvania, the situation could not arise where Socal, following the merger, would own stations next door to each other. It is, of course, possible that there may be a number of stations in Pennsylvania supplied by a Chevron jobber that are located on the same corner or very near a station owned or supplied by Gulf. If that turns out to be the case -- and we expect it would occur only rarely in view of the limited number of Chevron stations in Pennsylvania -- it might make good business sense for the owner or operator of one of the stations to change brands so that there would not be a conflict.

In today's market, we believe that whatever changes are necessary could be accomplished with little or no disruption. For this reason, we do not believe that it would be necessary to close any stations because of the merger, and that consequently the merger would not place any Pennsylvania service station jobs at risk.

QUESTION #2 In response to Senator Metzenbaum's question on lines 7 through 9 on page 125 of the transcript.

At the end of 1982, Socal had more than $10 billion in total liabilities. If the merger is approved, Socal would pick up Gulf's liabilities of $10.5 billion, and $13 billion in new liabilities as a result of the loan. This would amount to almost $34 billion in total liabilities. The Energy Daily reported that the merger "would boost Socal's debt share from 7 percent of total capitalization at year end 1982, the lowest among the majors, to 40 percent, among the highest." Are these figures correct, and if not, explain.

Socal had total liabilities including deferred income taxes and deferred credits of $9.9 billion at the end of 1983 (and $10.2 billion at the end of 1982). Gulf reported total liabilities including deferred items of $10.8 billion at the end of 1983 (and $10.5 billion at the end of 1982). Socal will add the fair value of Gulf's total liabilities to its balance sheet. The purchase accounting adjustments required for consolidation, including adjustments for Gulf's deferred income taxes, are expected to result in liabilities of about $9 billion. With the addition of debt incurred to acquire the common shares of Gulf of about $12 billion ($13 billion purchase price less Socal cash applied), total liabilities, including deferred credits and Socal deferred income taxes, will be about $31 billion for the combined companies. Total assets on the balance sheet will exceed total liabilities by $14 billion representing Socal's stockholder equity. Considering that the historical cost of Socal's assets as reported in financial statements is well below their fair market value, the total asset value for the combined companies is far in excess of liabilities.

With regard to the ratio of debt to total capitalization reported in the Energy Daily, we express the ratio as long-term debt and capitalized lease obligations to total long-term capitalization (total liabilities and stockholder equity less current liabilities). We have been quoting figures on this basis of about 10% for Socal prior to acquisition and in the 45-50% range immediately after acquisition. As we have stated, our intent is to reduce this ratio to the 25-30% range over the next several years, principally through the sale of certain assets.

Senator SPECTER. I would like now to call the fifth witness on the list, Mr. T. Boone Pickens, president and chairman of the board of Mesa Petroleum Co.

Mr. Pickens, if we are to apply the doctrine of equal time, you will have quite a lot of time.

Mr. PICKENS. It looks like we can go until 10 o'clock

Senator SPECTER. Well, we just might do that.

STATEMENT OF T. BOONE PICKENS, JR., PRESIDENT AND CHAIRMAN OF THE BOARD, MESA PETROLEUM CO., AMARILLO, TX

Mr. PICKENS. I have a formal statement here that I would like to present for the record.

Senator SPECTER. Thank you, Mr. Pickens, under our rules it will be incorporated in full and our practice is to ask for summaries, leaving the maximum amount of time for questions and answers.

Mr. PICKENS. I have 5 minutes for my remarks, is that correct, Mr. Chairman?

Senator SPECTER. Well, you have some leeway. There have been quite a number of issues raised.

Mr. PICKENS. I will stick to the time. It will not take me very long.

Senator SPECTER. Well, take whatever time you need. There have been a lot of questions raised and you have been mentioned with some frequency. I think as a matter of fairness, you are entitled to whatever time you need to respond.

Mr. PICKENS. Well, let me give you just briefly my background and what I believe qualifies me to comment.

Senator METZENBAUM. Could you hold the mike a little closer, Mr. Pickens?

Mr. PICKENS. Sure; let me just comment about my background that I believe qualifies me to discuss this issue.

I am a geologist by education and have been in the business for 33 years, exploration. I started Mesa Petroleum in 1956 with $2,500 paid in capital. And——

Senator SPECTER. When did you start again, Mr. Pickens?

Mr. PICKENS. 1956 with $2,500 paid in capital.

In 1964, we went public. Our assets were slighly less than $2 million at that time. I am not going to take you year by year. In 1984—we will jump forward 20 years—we have a company that has assets in excess of $2.5 billion now. And I might ask this question, if I might; do I sound like a liquidator at this point?

I have been characterized as that.

Senator METZENBAUM. You sound like a good potential political candidate. You have done well. [Laughter.]

Mr. PICKENS. Thank you. Thank you, Senator.

I also feel compelled to comment about Senator Johnston's remark that taxpayers were financing the purchase of our stock. I know that our bankers are going to be delighted to hear that they no longer have any liability there and the taxpayers are taking care of it.

I do believe in the free enterprise system. I feel I have been an active participant in this system for 33 years. And as to mergers and acquisitions in the oil industry, I come from a stockholder's viewpoint. That is exactly where I stand. I can see only winners in a transaction such as this.

I see the consumers coming up with a more efficient combination of two companies. I see the stockholders getting a price closer to appraised value. And remember here, Gulf Oil's appraised value is $114 a share. The stock was selling at $36 a share when we bought our first share. Today Socal has offered $80 a share for the stock. I see this as a healthy situation. I see tax revenues of almost windfall size to the Government of over $2 billion in this transaction.

To quantify my remarks and in conclusion, Socal is pumping $13.2 billion into the hands of 300,000 stockholders here. I think that is healthy. It goes right back into the economy. I see that there is no way competition is being diminished in any way. I see over $2 billion in taxes paid to the Government. And I see the consumer receiving a much more efficient industry combination.

And that, gentlemen, concludes my remarks. I am ready for any questions.

[Material referred to follows:]

T. Boone Pickens, Jr., president

MESA
PETROLEUM CO.

STATEMENT OF T. B. PICKENS, JR.

PRESIDENT AND CHAIRMAN OF THE BOARD

MESA PETROLEUM CO.

Mr. Chairman:

It is a pleasure to appear before you today. I thank you for affording me this opportunity.

Let me briefly summarize the points I intend to make today. First, the energy industry is in the midst of a major restructuring. This is a healthy development which is being led by shareholders, who have been largely ignored by the management of the major oil companies.

Second, mergers are an important part of this process that will promote efficiency in all aspects of the industry.

Third, there is no need to enact new antitrust legislation to prevent anticompetitive mergers since existing law is more than adequate, and as the Washington Post has noted, the concentration of ownership in the industry is low and oil markets are "genuinely open."

Fourth, mergers do not divert capital from drilling activity. Drilling activity has declined because of a lack of viable prospects, stable energy prices and high drilling costs--not a shortage of capital.

Fifth, anti-merger legislation only serves to entrench the management of the major energy companies, while it damages shareholders and consumers.

Sixth, consumers will benefit from mergers through more efficient management of the merged companies, the injection of new capital into the economy and the additional tax revenue derived from these transactions, which, incidentally, will reduce the federal deficit.

Seventh, as J. Paul McGrath, the head of the Justice Department's antitrust division, the SEC Advisory Committee on Tender Offers and others have noted, mergers do not adversely affect capital markets or the availability of consumer credit. In fact, as the SEC Committee has recently indicated, the problems in this area, to the extent they exist, are probably in the area of takeover defenses and not with acquisitions, per se.

Eighth, the enactment of merger legislation of any type could adversely affect not only the energy industry but also send shock waves throughout the stock market and create a dangerous precedent the exact impact of which cannot be fully measured in advance.

Finally, I must object to the form this bill takes, which appears to me to be retroactive antitrust legislation that singles out companies like Mesa. It would interrupt or terminate business transactions now in progress and would seriously harm thousands of shareholders. Mesa is acting to maximize shareholder values through legitimate and prudent actions.

Restructuring the Energy Business -- In the Public Interest

The energy business is in the process of being restructured as it struggles to replace reserves which are being produced. A healthy energy business is absolutely essential to our nation's security, and we must encourage the companies engaged in that industry to solve their problems with a minimal amount of government interference.

We interpret the scheduling of this hearing as an indication that your committee is dedicated to following a policy of judicious and careful consideration of any proposed legislation which goes to the heart of our free enterprise system. We believe that the committee is determined not to legislate by emotion or resolution, but by due process.

Mesa Petroleum Co. has received considerable publicity in recent months. We have been identified as a group of entrepreneurial people who are quick to seize upon an opportunity to benefit shareholders. We believe the shareholders are the cornerstone of corporate America. There are more than 42 million of these people who have invested in publicly held corporations.

We believe that managements frequently ignore their shareholders and easily forget that the shareholders are the owners of the corporation. They are the silent majority who accept abuses by managements and seldom protest. We are strong advocates of shareholder rights, and we make no apology for advancing these rights wherever possible. We are willing to protest when these rights are ignored.

In this capitalistic society, these are our constituents, Senators, just as we are your constituents. Among this constituency are many voters. Elected officials, as well as corporate managers, should listen to these people.

We know something about preserving shareholders' rights. We also know something about mergers and acquisitions and exploring for and finding hydrocarbons. In verification of these statements, allow us to tell you something about our company.

Mesa Petroleum Co.: Increased Efficiency Through Maximizing Shareholder Value

Petroleum Exploration Inc., the predecessor company of Mesa, was capitalized with $2,500 in 1957. Five years after Mesa emerged as a public corporation in 1964, we tendered for and acquired another public corporation engaged in the production of hydrocarbons. This company was 20 times the size of Mesa. It had large gas reserves, considerable cash flow and no exploration staff. It was destined to deplete its reserves in a matter of years, which meant the stockholders would deplete their reserves and income while the employees ended up with no jobs.

This company was quickly assimilated into Mesa where the cash flow was directed to expanding our exploration activities, employing highly competent scientists and building the reserve base for our shareholders. Three years later, we acquired another energy company and the procedure was repeated. In each instance, efficiencies of operation were greatly improved, the return on stockholders' investments was enhanced. No people were laid-off. Some few employees elected to resign rather than move to new locations.

Also, in each instance, the shareholders of those companies merged into Mesa who elected to take Mesa stock in exchange for

their original shares enjoyed significant appreciation in both market value and asset value.

We proved that through acquisitions, a larger, more profitable and vital company could emerge. We also demonstrated that through expanded exploration budgets made possible by the larger cash flows and borrowing base of the combined companies, more oil and gas could be found.

Since its inception in 1964, Mesa has replaced and enhanced its reserve base. Replacement has been achieved primarily through intensive exploration and development. During the last five years, total additions to Mesa's liquid reserves represented 139 percent of production and additions to natural gas reserves represented 187 percent of production.

We are proud of this record; we are less proud of our cost in finding oil and gas in recent years. Industry-wide, the high cost of finding hydrocarbons is the most serious problem facing management.

The most recent data covering the Fortune 500 companies shows that Mesa would be included in the top five energy companies in assets and net income per employee, and in net income as a percent of stockholders equity. An investor who purchased 1000 shares of Mesa for $10,000 when the company was founded in 1964, as a result of the stock splits and the creation of two royalty trusts, would now have a market value of approximately $240,000.

Our management has been recognized for its ingenuity, its expertise in finding oil and gas, and its dedication to the shareholders. We have been selected as the best managed among 89 companies in oil and gas production, and the Wall Street Transcript indentified me as the best chief executive among oil producers in 1981 and 1982. Last year Financial World selected our annual report as one of the three best among companies in the petroleum industry.

Mergers Do Not Adversely Affect Drilling Activity

The oil and gas business is a highly competitive industry. We have had both good and bad times. Today, the domestic energy

business is in trouble. Oil and gas reserves are being depleted faster than they can be replaced. In the last three years, the largest oil companies have averaged replacing less than 66 percent of the amount of hydrocarbons they have produced in the United States. There is a serious question whether or not the current price of crude affords sufficient economic incentive to explore in frontier areas, and the natural gas market is saturated. Consequently, the number of drilling rigs being used in exploration and development continues to decline. In other words, the drilling decline is not caused by a shortage of capital.

I see no reason why a merger should be barred when it can be structured to benefit shareholders and meet the very rigid requirements of existing antitrust laws and other applicable statutes. I submit that if a more efficiently managed merged company reduces its exploration budget - for whatever reason - that will only create more opportunity for independents: the real risk takers in the energy business who already drill 80% of the exploration wells in the domestic U.S. To block mergers in an effort to force increased drilling makes neither good economic or energy policy sense.

Mergers Have No Adverse Impact on Capital Markets

To say that these mergers drain the resources of this nation and result in a shortage of bank credit generally available to individuals and businesses just is not true. This is a fallacy that is discredited by the recently publicized report of the Securities and Exchange Commission Advisory Committee on Tender Offers. Based on its own experience and study, and supported by Federal Reserve Board Chairman Paul Volcker, the Committee notes that transactions involving acquisitions of control do not distort the credit markets or divert investment from new plants, nor do they limit consumers' ability to obtain credit or deplete credit otherwise available to would-be borrowers. Moreover, the SEC Committee explained that takeover transactions fundamentally involve a transfer of existing assets, not the absorption of new savings, and because the shareholders who sell their stock to an acquiring firm typically reinvest the proceeds, the capital

remains in the economy and is made available to others. And these shareholders pay taxes, big taxes.

To recap, U.S. financial institutions are awash in liquidity. There is no undersupply of credit. The problem is a scarcity of good drilling prospects, and the depressed price of oil and gas gives little incentive to the explorer. Ample capital is available for viable exploration prospects.

As stated previously, shareholders should have the option to direct companies to merge when circumstances warrant. Artificially protecting management from the prospect of having to merge removes one more valuable shareholder's right and further insulates insensitive officers from the concerns of their shareholders.

Mergers Do Not Hurt Consumer Prices

The new company will not suffer any diminution in its ability to look for oil and gas, and quite likely will be more operationally efficient; thus, prices of gasoline at the pump will not be adversely affected. Gasoline prices are tied to the price of crude oil and OPEC sets that price. Economic factors within the industry, not mergers, generally dictate the level of employment, and the employment or dismissal of people depends upon the national economy and the profitability of the company. To achieve a higher level of efficiency in a merger, some jobs may be lost; but, this in itself cannot be the primary reason for Congress to legislate against the right of corporate owners -- the shareholders -- to elect to merge. This right, exercised within the restraints imposed by reasonable laws, carefully designed to protect the national interest, must be retained.

Retroactive Antitrust Legislation: Inequitable Policy and A Dangerous Precedent

Finally, we find it to be totally contrary to the free enterprise system when Congress considers changing the rules under which thousands of shareholders invested in energy companies and threatens to tell these people that they are going to be denied the right to enjoy the fruit of their labor and the profit from their investments. If statutes governing mergers and acquisitions are to be amended, they should be amended only after

careful and deliberate inquiry, and they must not be changed with regard to business transactions then in progress.

You are at the brink of legislating out of existence a part of the initiative, the determination and the entrepreneurial spirit which is the bedrock of our free enterprise system. This is an awesome responsibility, and I urge you to be most deliberate and cautious before summarily administering a coup de grace of that magnitude.

Should you have any questions which may arise as a result of my testimony or the testimony of other witnesses, I would be most happy to appear before you again.

THANK YOU.

T. Boone Pickens, Jr., president

MESA
PETROLEUM CO.

March 16, 1984

The Honorable Strom Thurmond
President Pro Tempore
218 Russell Senate Office Building
Washington, D.C. 20510

Dear Senator Thurmond:

I am writing this letter because I may have misinterpreted one of your questions at the Senate Judiciary Committee hearing on mergers and acquisitions yesterday and I think it best to make my position clear.

Your question was whether I believed it appropriate for the oil industry to be concentrated into a few companies. My answer is unequivocally no. Fortunately that is not now the case. While Mesa Petroleum, although far down on the list and not a major, has never had any difficulty competing with the top oil companies, it is my belief that the present antitrust laws are adequate to ensure that the oil industry will never become over-concentrated.

Sincerely,

Boone Pickens

T. Boone Pickens

ONE MESA SQUARE / POST OFFICE BOX 2009 / AC 806 / 378-1000 / AMARILLO, TEXAS 79189-2009

Senator SPECTER. Mr. Pickens, according to Mr. Pertschuk's written testimony, in lining up credit to bid for Gulf, Mesa's capital spending plans for 1984 had to be cut in half. What impact, if any, did this have on Mesa's exploration and drilling programs?

Mr. PICKENS. Well, Senator, if I might, allow me to take you back to the high watermark as far as Mesa's budget size was concerned. And Mr. Keller mentioned that there would not be anybody to loan money for exploration drilling. I believe that was his quote 2 hours ago.

In 1981, which was not inconsistent with prior years at Mesa Petroleum, we had borrowed money for exploration. We ran a budget of $420 million with a cash flow of less than $200 million. So we were borrowing two to one on cash flow.

As we came down from 1981 to 1982 we had a $320 million budget, still well in excess of cash flow. The 1983 budget was $223 million; it was the first time in the history of Mesa Petroleum that we were now operating on cash flow. That was our cash flow.

In 1984 we have dropped our budget to $100 million, which is about 40 percent of cash flow, which is in line with Socal and Gulf, which operate on a domestic budget of about 40 percent of their cash flow for their domestic exploration So we are in line with the rest of the industry at $100 million.

Senator SPECTER. Mr. Pickens, what is your response to the charge that your effort at Gulf is an effort of a predatory acquisition?

Mr. PICKENS. Well, I find it to be interesting because I thought we were working in behalf of all the Gulf stockholders. And when Mr. Lee says that if they had a stockholders' meeting we would displace Gulf management, it makes me think the owners of the company are not too happy with management.

But I do not see us as a predator. We saw undervalued assets here and our opening statement when we bought the Gulf stock was that we would attempt to maximize values for all the Gulf shareholders. I think that has been accomplished. I cannot quarrel with Socal's offer of $80 a share. That is better than our offer. We still have an offer out there for $65.

And remember the all time high for Gulf stock was $54. So our offer is still well in excess of what the Gulf management was ever able to do for their shareholders.

Senator SPECTER. Mr. Pickens, did you in fact plan to liquidate Gulf?

Mr. PICKENS. I did not plan to do that, and the document that Mr. Lee continues to wave up in the air here, that that was a liquidation plan of Pickens, it was not a liquidation plan of Pickens.

Senator METZENBAUM. It was not what?

Mr. PICKENS. It was not a liquidation plan of Pickens.

Senator SPECTER. If you had gained control of Gulf, what changes would you have instituted in Gulf's research, exploration, and drilling efforts?

Mr. PICKENS. If you went back over the record, you would see that we never intended to take over Gulf Oil. We did not want to take over Gulf Oil. But we got to a point where we then had to go ahead and move in that direction. And that was sometime in February.

But I told Bill Wiley with the Pittsburgh Press when he asked: "What will you do if you do displace the Gulf Board of Directors?" that my wife and I will move to Pittsburgh and I will work like hell.

But that is not unusual for me. I do work hard. And we would have done a good job at Gulf Oil. But that does not seem to be in the cards and that is fine because I think Socal's offer is better for the stockholders.

Senator SPECTER. Mr. Pickens, if the Gulf-Socal merger goes through, will you not have a new company which will have a stock value substantially less than book value?

Mr. PICKENS. If Socal and Gulf——

Senator SPECTER. Socal and Gulf.

Mr. PICKENS. I have not really studied the combination of those two companies. I think that when I look back over at an appraised value of $114 and that Socal is offering $80, that is about 75 percent of appraised value, and that is in line with the Texaco offer for Getty. It's appraised value was $153 and it went out at $128. Royal Dutch has offered $55 for the Shell Co. and the appraised value is $69. So $80 is a little on the low side, but it is in line with the other deals.

I assume that Keller and his group are very capable people. Socal is a fine, large company and they know what their assets are and they know what they can handle.

Senator SPECTER. Would a new merged company of Gulf-Socal be a good target for a Boone Pickens-Mesa takeover?

Mr. PICKENS. Well, I am up to my neck in a deal right now and I have not really thought about any other deal.

Senator SPECTER. You have not thought about that one?

Mr. PICKENS. I have not, but I can tell you, Senator, that I get frequent letters from stockholders that say, have you thought about our company and would you consider coming in and being a stockholder of our company in getting something started.

And so I find that to be interesting. And I do relate very well to stockholders. I have no problem with that.

Senator SPECTER. Let me ask you a couple of questions about changes in the law concerning how they would affect you, before turning it over to Senator Metzenbaum.

You probably heard a question that I asked earlier relating to a recommendation by the SEC advisory committee, that anyone who wanted to acquire more than 20 percent of a class of equity stock in a corporation would be compelled to acquire the entire corporation. It could not get more than 20 percent. How would that affect your ability to take over a company like Gulf or a company like Socal-Gulf?

Mr. PICKENS. I do not know. I have not had an opportunity to study those new suggestions on the part of the SEC. It has not been something that has been high on my list of priorities.

OIL-DEPLETION ALLOWANCE

Senator SPECTER. What is your reaction to the charge that your ability to undertake these takeover offers has been really a result

of the extraordinarily favorable tax treatment that you have received as an oil company?

Mr. PICKENS. I do not see any merit at all to the argument that takeovers are related to the tax treatment we receive. I think that Senator Hatch's comments earlier about how much taxes we would pay in this deal, were that it would be substantial.

Senator SPECTER. I am talking about the depletion allowance which the oil industry has had and the tax shelters that enable you to acquire cash and put you in a position to move into takeovers.

Mr. PICKENS. I do not think the depletion allowance has anything to do with these types transactions.

Senator SPECTER. Well, it puts more cash in your pocket. It is a form of a tax shelter, is it not?

Mr. PICKENS. Well, I do not see depletion as a tax shelter. I feel like those particular tax laws are in place and that they are necessary for the industry to operate—remember, again, this industry is having a tough time right now. I do not see how the tax laws were ever a factor in any acquisition.

Senator SPECTER. Mr Pickens, what effect would there be on your ability to take over a company like Gulf if there were a change in the tax laws related to the dividends received credit or if there were a new definition that you could not deduct interest payments or if there were a new rule as to capital gain treatment after liquidation?

Mr. PICKENS. I think that would certainly be a factor in looking at any situation.

Senator SPECTER. Would it put a pretty big crimp in your sales?

Mr. PICKENS. Pardon me?

Senator SPECTER. Would it put a pretty good crimp in your sales?

Mr. PICKENS. It would change the economics if you did not have the dividend carry and you were not able to deduct interest.

Senator SPECTER. Do you think it would stop you from taking over a company like Gulf?

Mr. PICKENS. Well, I think if we are going to come down to something like this, that we better start putting a legend on these stock certificates like a cigarette pack, that says beware, if you keep smoking these, they will kill you. I think you had better put this legend on the stock certificates because when people see these undervalued assets and they see an opportunity to upgrade those values, if you take it away from them, it should be identified that way.

We are not talking about liquidating anything here, either.

Senator SPECTER. Well, Mr. Pickens, I do not think the Congress wants to take any action which is going to inappropriately impede transferability of stock or make the market difficult for shareholders to get higher values.

What we are concerned about are underlying public policy considerations. And the worry we have is that we see transactions going on where $15 billion is isolated off to the side in a very difficult credit market with very high interest rates; Government has very heavy borrowing, et cetera.

Then we see a consequence where companies are acquired because their reserves are valued much less than exploration would cost. The object from a public policy point of view is to structure

the laws to encourage exploration and not to encourage transactions which are manipulative and do not encourage exploration or the development of natural resources.

That is where our concern is. Are we wrong in our thinking in trying to put a stop to the kinds of activities that are posed by your efforts at Gulf?

Mr. PICKENS. I think so, yes.

Senator SPECTER. Well, how would you respond to this issue about all of this money being isolated that serves no real public policy purpose?

Mr. PICKENS. It does serve a public policy purpose. You are talking about here, $13.2 billion going into the hands of 300,000 stockholders and 2 billion dollars' worth of taxes being paid; I think that does serve a purpose.

Senator SPECTER. Does it not discourage exploration when you do not have to go out and drill for new oil reserves, but can buy them?

Mr. PICKENS. I do not think so. You are going to have to look at the rig count. We had a high water mark in the third week of December 1981 of rig activity in the United States with 4,531 rigs running. In April 1983, we sunk to an 1,807 rig count. Today we are operating 2,250 rigs in the United States. That is about half of the 4,500 rigs that we had running back in 1981.

The rig count will go up when the finding costs come down. When the prospects are there the people will explore. As far as Socal buying Gulf, that is a stand-alone deal as far as I am concerned and I completely agree with Mr. Keller. He will run a budget that is equal to the combined Gulf-Socal companies.

But in the event that they decide that they do not want to run a budget that size, there are other people around that are quite willing to drill those prospects. The oil is not going to go anyplace. This oil has been in place for hundreds of millions of years. And it is there to be discovered. So if we do not find it today or we do not find it next year, we can find it the next year or the next year.

So there is no problem here.

Senator SPECTER. Senator Metzenbaum.

Senator METZENBAUM. Mr. Pickens, I think you have gotten sort of a bad rap.

Mr. PICKENS. Thank you.

GULF INVESTORS GROUP

Senator METZENBAUM. I really do; you are called predatory. I think it is a perjorative term. I think you did what the free enterprise system permits. If we do not like it in Congress, if we think it is not in the country's interest, I think we are supposed to do something about it. But I think you used your head and you saw something that was out there and you went out and you bought it; you bought the stock.

And so I do not have any fault to find with that. I do have some concerns, however, about the ultimate end, and that does not relate to you being able to make a good business deal. It concerns me as to impact upon the economy, impact upon oil reserves, impact upon the consumers. Let me first ask you, you speak for yourself and

who else? Can I ask you who else is in your total group? As I understand it you speak for more than yourself.

Mr. PICKENS. Yes. I represent the Gulf Investors Group, I cannot give you the legal identities of each one of them. Could I just identify them as people?

Senator METZENBAUM. Sure. I understand that.

Mr. PICKENS. John Harbert, who operates as Harbert International. And we have Sunshine Mining. We have the Belzbergs, Sam and Bill Belzbert. And the fourth entity is Wagner and Brown, Cy Wagner and Jack Brown from Midland, TX.

Senator METZENBAUM. And is not Penn Central in?

Mr. PICKENS. Penn Central is not a partner in the deal. Penn Central just provided financing. We made a financing arrangement with Penn Central. They are not a partner in the Gulf Investors Group.

Senator METZENBAUM. I see. Now, you said something today that is totally opposite the national public perception, at least those who are on the national scene who have some concern about this matter and some awareness of it. You said you have no intention of liquidating. How did it come about that this was—how does it come about that everybody talks about the fact that Boone Pickens takes over Gulf, he is going to liquidate the company. He is going to open a royalty trust.

Could you tell me how that came about and what the actual facts are and what your intent really is.

Mr. PICKENS. I am not sure that I have the facts of how I got identified as a liquidator. But let me back up to the original purchase in October. And at that time our pitch was to take—let us identify Gulf for what it was at that point; the company was in liquidation.

Senator METZENBAUM. It was what?

Mr. PICKENS. The company was in liquidation. Gulf Oil was in liquidation. They had had 12 straight years of down domestic reserves, which I think you would agree with me is a trend. If they had taken their own points out of their own annual reports and lined them up, Gulf Oil would have had no more domestic oil in 1995. Now, I know the curve flattens out and it looks a little better than that someplace out there, but the fact is it would have been too late for the stockholder.

For 10 straight years Gulf Oil increased the dividend and along with it most of their salaries. Somehow they identified salaries with dividend increases instead of exploration success.

But we saw the company in liquidation. We saw the appraised value at $114. And we could see that they were up to their neck in cash with a projected $3.2 billion in cash flow for 1984. We felt like it was only fair to share a portion of that cash flow with the stockholders. And so we made the royalty trust proposal. We asked them to spin off about 25 percent of their reserves to the stockholders. We did not ask to go on their board. We did not want to run their company. We did not want to get involved other than to share a portion of the cash flow before Gulf was liquidated. That was the royalty trust concept.

Now, the liquidation came from an idea that our investment bankers came up with and I think that is the document that Mr.

Lee was waving around there two or three times; that was not a plan of ours. It was never passed on. I never accepted it. I never left the royalty trust concept. I was still talking to Mr. Lee about the royalty trust concept on January 26 in his hotel room in Pittsburgh. And the following week was when Arco floated the $70 offer in there.

So what I was interested in was a portion of those reserves being shared with the stockholders before they were liquidated.

Senator METZENBAUM. If you shared 25 percent of their reserves, what impact would that have on the company?

Mr. PICKENS. I would think it would have a positive impact because the combination of the two pieces of paper, I felt, would bring the market value to the stockholders to $70 a share. So I thought it was a very positive impact. Of course, we were their largest stockholder. We did not want to do anything to hurt them.

Senator METZENBAUM. What you would have done is to spinoff, to liquidate 25 percent of their reserves into a royalty trust; is that what you are saying?

Mr. PICKENS. Well, you said liquidate and again that makes me a little jumpy.

Senator METZENBAUM. I changed it. I said to spinoff.

Mr. PICKENS. That is right.

Senator METZENBAUM. You would—what was your plan?

Mr. PICKENS. Yes; they had $3.2 billion cash flow and we wanted them to spinoff about $700 million, which would leave them $2.5 billion, and their domestic exploration budget was $1.5 billion. So they had plenty of coverage for exploration drilling.

Senator METZENBAUM. Now, if Socal were stopped in its efforts, and I know that you made it very clear that you are not here advocating that position, but if it were stopped in its effort and if you were then in a position to elect a new board, what would be your plan and what would you do with the company?

Mr. PICKENS. At that point, I would move to Pittsburgh. I have no idea of moving operations out of Pittsburgh or closing down any of their operations. I think we would go in and look at them very closely, determine those that we felt were good, solid profit centers, and stay with them. But if we did not stay with them somebody else would be running these operations. Somebody else may be able to run them better than we would or Gulf management would be able to.

We are not talking about going out here and wiping out a refinery or something like this. That is not in the best interest of stockholders.

Senator METZENBAUM. What I am really asking you now is, If you were able to elect your board of directors or a majority of the board of directors, would you then spinoff the reserves or would you go in and try to run the company?

Mr. PICKENS. Well, wait a minute. We would run the company. I mean, we may spinoff reserves, but we believe that would make the company more efficient. We are talking about sharing cash flow with owners. This is not like we are going out and just tossing this money out the window. I am stumping for stockholders at this point.

I do not want to see those natural gas and oil resources depleted without having the reserve base maintained. I say bring the reserve base down to a level you believe you could maintain it at and then share the cash flow with the stockholders with the other part of the reserves.

We are not talking about letting any people go here, either. When you spinoff these assets, you still keep total control of them. The company still has 100 percent of the working interest.

It is only subject to a portion which would be net profits or net royalty interest.

Senator METZENBAUM. Well, let me change the subject, then, for a minute. You indicated that if the Socal-Gulf merger were to occur, I think you said something about the consumer would benefit because you had come up with a more efficient company and that you did not see competition being diminished.

Now, I may be misquoting you.

Mr. PICKENS. That is basically what I said, yes, sir.

Senator METZENBAUM. Tell me how you explain that. Because as I look at it, if you are using your dollars to pay off your debts, if you do not have your dollars to go out and explore for new oil, that hurts. If you have less competition in the effort to develop and find new oil, there is not more competition, there is less competition.

And it would seem to me, at least from my perspective, that the consumer will wind up being hurt because if there is less oil, then obviously the price goes up.

Mr. PICKENS. Well, the consumer is going to be hurt if you have an inefficient operation because eventually inefficiency is going to have to be digested through the system and that means the consumer is going to have to pay. So in the combination of these two companies, there will be efficiencies gained. As far as the price for oil, Socal does not have any more control over the price of oil than Mesa Petroleum has. That is controlled by the OPEC cartel.

Again, the oil is not going to go anyplace. If we can find it for a reasonable cost, that is good. If we cannot find it for a reasonable cost, then we are inefficient. And that is going to have to be digested someplace through the system.

Also, the industry is so fragmented; I believe the Socal-Gulf combination will be less than 5 percent of the oil reserves in the United States.

Senator METZENBAUM. How do you say that they would be more efficient. So they save some on the rent; they save some on some employees. But by and large they would not be saving that much. How do you explain your point that they would be more efficient if the two companies were merged?

Mr. PICKENS. I think, again, it is a tough question for me because I am getting into the downstream operation where I do not have that kind of experience. If I can speak in the upstream operation, I feel more comfortable. Socal has been a better explorer than Gulf has. Their finding costs are lower. Their replacements are higher. The combination would be vastly different as far as efficiency for the stockholder and the consumer in the upstream operation.

Senator METZENBAUM. That is sort of a speculative idea, that Gulf has done it well in the past, as you pointed out, though. You say they are good in finding new reserves, and yet you have also

indicated that their reserves have been going down consistently for the last 10 years.

Mr. PICKENS. I may have been misunderstood there. I said that Socal has done a good job of finding, a better job than Gulf has.

Senator METZENBAUM. Oh, I thought you said Gulf.

Mr. PICKENS. No, I said Socal. Socal has done a better job finding oil than Gulf has.

Senator METZENBAUM. All right. If they go through and complete their deal, Socal is going to have less dollars available for the purpose of exploration. You just cannot cut it any other way there. The assets to debt ratio is certainly going to be impacted very drastically.

Mr. PICKENS. Well, I have to go along with Mr. Keller's comments on that. I feel that Socal has looked at this deal very closely and they know exactly what they are doing. I believe Mr. Keller sitting here saying that he is going to run a budget, an exploration budget, that would be equal to the combined companies, and that he has financed this in a way that he can take care of the amortization of the debt. I believe him to be honest in his remarks there.

I cannot speak as an expert on the Socal-Gulf combination. Even though we are Gulf's largest stockholder, they have not invited me in to see all the things that they might. I really have not been included.

Senator METZENBAUM. They have a welcome mat out in front of the door, I am sure.

Mr. PICKENS. I have missed it somehow.

Senator METZENBAUM. Thank you, Mr. Chairman.

Senator SPECTER. Senator Nickles.

Senator NICKLES. Thank you, Mr. Chairman.

Mr. Pickens, a couple of questions. Again, a lot of us have heard that if the Pickens Group was successful with Gulf, Gulf would be liquidated. You said that is not true. You did say you would spin off a certain percentage of the reserves for income for stockholders. Would it be your intention to shut down the major refinery in Philadelphia and other major refineries? Would it be your intention to shut those down and try and spin those off to reduce your debt?

Mr. PICKENS. Senator Nickles, the debt would not be that much of a factor. We would own 21 percent of the company. And that debt can be managed very easily. Now I hope I was not misunderstood again, I did not say that if we did take control of Gulf, that we would spin off a royalty trust.

I said that would be one thing we would consider. What we had asked Gulf's management to do was to spin off 50 percent of their domestic reserves, which represent 25 percent of their cash flow, to the stockholders. But I am not proposing that that would be the case here at this point, that if we did elect our board of directors, that that is what we would do.

And as far as the Philadelphia refinery is concerned, again we would go back and look at those operations very closely and decide which ones were making money and which were not making money.

Senator NICKLES. You probably heard Senator Johnston's response to a question that I had asked earlier. I can see a scenario

happen if this legislation were passed where you with your existing ownership of Gulf, being the largest shareholder, unless it was crafted differently, would have effective control of Gulf. Now, that is one possible scenario. It may be right; it may not be right. I do not know what would happen at the end of the moratorium.

But it is a possibility. Is that a possibility that you hope would happen or as a stockholder would you prefer the Socal-Gulf merger being able to be completed?

Mr. PICKENS. Well, Senator Nickles, I found it to be interesting to hear Mr. Lee's testimony here today, that if they had a stockholders' meeting, I think he said it would not be in the best interest of 259,995 stockholders if it went to the Pickens Group or however he styled it.

But he said also that he would lose a proxy fight if that did come up, which I find to be interesting. Why are the stockholders so stupid that they would vote for the wrong slate of directors? I find that to be interesting. And here again I think that the democratic process that we all live under, thank God, that that is the stockholders talking.

Senator NICKLES. A couple of quick questions. We have heard a lot of people refer to possible tax changes. Senator Specter alluded to it earlier. As a major integrated oil company does Gulf have percentage depletion allowance on oil?

Mr. PICKENS. Does Gulf have percentage depletion?

Senator NICKLES. Gulf Oil.

Mr. PICKENS. I am sure they do, yes.

Senator NICKLES. Not as a major.

Mr. PICKENS. They do not have as a major?

Senator NICKLES. No, they do not.

Mr. PICKENS. I did not know the answer, obviously.

Senator NICKLES. I probably should have asked the question in a different manner. The point I wanted to make is that a lot of people who are talking about the special tax benefits that big oil receives do not necessarily have the facts straight. I think it is important to note that big oil does not receive a percentage depletion, and all other minerals do, including coal.

Almost every other mineral does have its percentage depletion. Independents do. I do not know how Mesa is classified, whether Mesa would still be classified as an independent or a major?

Mr. PICKENS. I do not think we are identified as a major.

Senator NICKLES. You keep being successful and you will be. But I think this is an important point. One other thing that is important on this tax question, when we talk about the tax issues everyone should remember that the oil industry is the only industry which has a windfall profits tax, which for the last couple of years has exceeded 30 percent of all the corporate income tax combined, including corporate income taxes paid by oil companies. So, yes, there has been some discrimination in the past, but it has not been for special benefits for oil. It has been a negative benefit from the fact that it is the only industry that has a windfall profits tax.

The legislation would basically—as I see one of the amendments dealing with royalty trust—would be an amendment to pick on Pickens. It would be an amendment to eliminate the possibility of a royalty trust taking control of over 5 percent of any company.

It would be an amendment that would eliminate your adventurish or your expansionistic endeavors to purchase other companies. Do you have any comments on being almost singled out by that type of legislation?

[Senator Thurmond resumes the Chair.]

Mr. PICKENS. I feel like I have cross hairs between my eyes. I think the gun is pointed right at me.

Senator HATCH. Did you call this predatory legislation?

Senator JOHNSTON. Yes.

Mr. PICKENS. Thank you.

Senator NICKLES. Thank you. Thank you, Mr. Chairman.

The CHAIRMAN. OK. Have you examined the witness yet?

ROYALTY TRUST

Senator JOHNSTON. No. Thank you, Mr. Chairman.

Mr. Pickens, it may be predatory legislation, but as I told you privately I am a great admirer of yours. I really think you represent the best the free enterprise system has to offer. I really do.

Now, you say you are not a liquidator, but you would set up a royalty trust. Is a royalty trust a form of liquidation?

Mr. PICKENS. Is that my question?

Senator JOHNSTON. Yes, sir.

Mr. PICKENS. Senator, again I did not say that we would set up a royalty trust. I asked the Gulf management to do that because Gulf management was liquidating the company. It had not replaced its domestic reserve base for 12 straight years.

Senator JOHNSTON. Is a royalty trust a form of liquidation?

Mr. PICKENS. Well, when you say a form of liquidation, it is a normal depletion of the reserve base, yes.

Senator JOHNSTON. And it is, to be fair, it is a form of liquidation.

Mr. PICKENS. It would be liquidated over a period of time; that is correct.

Senator JOHNSTON. All right. Now, you were not required in your SEC filings to state what you are going to do, but you did put out, I think, a gray book to the Gulf shareholders stating what your intention was, did you not?

Mr. PICKENS. A gray book to the——

Senator JOHNSTON. I think they call it a gray book. Maybe it was a different color.

Mr. PICKENS. I do not remember ever putting anything out to the Gulf shareholders called a gray book.

Senator JOHNSTON. The Mesa investors, did they not say what they would do? Did you not give it to the Mesa investors or what do you call them, the Gulf stockholders group?

Mr. PICKENS. The Gulf Investors Group?

Senator JOHNSTON. Right.

Mr. PICKENS. That is made up, you know, of like five or six people. It is not the Gulf stockholders.

Senator JOHNSTON. Did you not give them a gray book or some instrument saying what your plan was?

Mr. PICKENS. I do not recall a gray book being given to them, Senator. I am not trying to be evasive, but are you referring to the one that our investment bankers came up with?

Senator JOHNSTON. I was told that there was a gray book given to your group stating—or given to some group stating what your plans were when you took over Gulf, and that that involved creating a royalty trust.

Mr. PICKENS. No, I do not recall.

Senator JOHNSTON. You testified here that you had in mind with respect to Gulf if you got control, to set up a royalty trust involving 50 percent of the reserves and 25 percent of the cash flow. Did you not just say that?

Mr. PICKENS. No; I am sorry if I am confusing you. What I said was we asked the Gulf management to spin off 50 percent of the reserve base, the domestic reserve base, and 25 percent of the cash flow.

Senator JOHNSTON. If you asked them to do it, then that is what you would have done or what you will do if you get the chance?

Mr. PICKENS. Well, I am not ready to make that commitment here because we have not even filed our proxy material. So you are asking me to preempt that proxy material. We have not made that decision as to what our plan would be.

Senator JOHNSTON. Would I be reasonable in thinking that if you asked the Gulf management to do that—you said, do that, it is in the interest of the stockholders, that if you had a chance to do it, you would do it. Would I be reasonable in thinking that?

Mr. PICKENS. I do not think so. I think that is one of our options. I am not trying to be difficult, I promise you. We have other options that we are considering at this time. That just happens to be one of them.

Senator JOHNSTON. Now, we have established that a royalty trust is a form of liquidation and that you asked the Gulf management to liquidate half their reserves.

Mr. PICKENS. No, I did not ask them to liquidate; I asked them to share 25 percent of the cash flow with the owners of the company. That is what I asked them to do.

Senator JOHNSTON. Well, you asked them to put it in a royalty trust, which you now say is a form of liquidation.

Mr. PICKENS. That is right, but the company is in liquidation because it has not replaced its reserve base for 12 years. Let me give you an example. In the last 5 years——

Senator JOHNSTON. I understand——

The CHAIRMAN. Will the Senator let him finish his answer.

Mr. PICKENS. In the last 5 years Gulf has depleted from the reserve base and not replaced the equivalent of 634 million barrels of oil. Now, that is a company in liquidation if you let 634 million barrels of oil equivalent get away from you in 5 years.

Senator JOHNSTON. Well, I know, but the country is in liquidation because we have lost 17 percent of our reserves as a nation in the last 10 years. So everybody is in liquidation by that definition.

Mr. PICKENS. Yes; and that is why I kind of hate to see you single out that a royalty trust is in liquidation too because Gulf Oil is in liquidation. So we are in agreement on that.

Senator JOHNSTON. We are in agreement that a royalty trust is a form of liquidation, that you asked Gulf to liquidate half their reserves I think they are right when they say you are a liquidator. Now that may be good or bad, but I think they are dead right

Let us get to Mesa. What is Mesa's exploration budget now as opposed to what it was in 1981.

Mr. PICKENS. It was $400 million-plus in 1981. In 1984 it is $100 million.

Senator JOHNSTON. It is 25 percent of what it was. And what has happened in the meantime? You have created a royalty trust.

Mr. PICKENS. No; we created a royalty trust in 1979. The biggest budget we ever had was 1981. At $100 million we are running 40 percent of cash flow, which is in line with and comparable to Socal and Gulf.

Senator JOHNSTON. You are coming down to 25 percent of what it was.

Mr. PICKENS. Pardon me? We were borrowing $200 million in 1981 to drill wells. Mr. Keller said that there would not be anybody who would do that. That makes me wonder about my judgment as a CEO of an oil company.

Senator JOHNSTON. Now, Mr. Pickens, you and I had a good talk and we agreed on a whole lot of things. And one of the things you told me, as I recall—check me if I am right—was that you think oil companies are spending too much on exploration right now, that there are not that many good prospects left in the country. Is that not right?

Mr. PICKENS. No, that is not what I said, Senator.

Senator JOHNSTON. What did you say?

Mr. PICKENS. I said that there is plenty of cash flow in the United States today in the domestic oil and gas industry to drill all the drillable prospects. There is plenty of cash flow there. We are not taking any cash flow out that is going to cost us any wells to be drilled.

Senator JOHNSTON. Well, any good wells, and what you are saying is that they are drilling too many wells that are not good wells today? They are wasting money on it. They ought to cut back and there is plenty of money to the cutback figure. That is what it amounts to, is it not?

Mr. PICKENS. Senator, I am not so sure that I remember those things in our meeting. In fact, I am not commenting about other people, whether they spend their money on good wells or bad wells. I can talk to you about Mesa Petroleum.

Senator JOHNSTON. Well, I will not go and try to reconstruct that.

Let us talk about all these stockholders. How many did we say we had?

Mr. PICKENS. I said 270,000. I have a stockholder list that Mr. Lee gave me. I do not know why I have 270,000 and he has 259,995 he said. So let us call it 265,000. We will split it with him.

Senator JOHNSTON. I do not know if you saw that Wall Street Journal article by Charles McCoy and Christian Hill, but they detailed the history of your takeovers and they say this:

None of these transactions resulted in Mesa gaining control of its target and implementing a royalty trust or any of the other restructuring devices Mr. Pickens has

championed. The biggest winners in his raids are often speculators, not the small shareholder he professes to hold so dear.

Is that right?

Mr. PICKENS. No, it is not right.

Senator JOHNSTON. Now, as a matter of fact, when—if the deal goes through here at $80 and I understand that at least the story is going around that somebody called you up on the telephone and said Socal was just offered $80 and you said, shucks, lost another one. Is that right?

Mr. PICKENS. That is not right.

That was in Business Week and I have never used "shucks" in my life. [Laughter.]

Senator JOHNSTON. Well, that made a good story anyway.

I understand that about a third of the total shares in this big takeover would go only to your group plus another 10; is that right?

Mr. PICKENS. Pardon me?

Senator JOHNSTON. A third of the total biggest paychecks, according to this same Wall Street Journal article would go to your group, which would get $1,738.8 billion plus another 10, including the arbitragers, $1,600,000. In other words, a few people, your group plus about another 10 would get about a third of the total dollars here.

Mr. PICKENS. No. That is not the way we see it. We believe 75 percent of the $6.6 billion profit that we see in the deal would go to the long-time holders of Gulf Oil.

Senator JOHNSTON. Well, I am sure the Mellon Group has been a long-term shareholder, have they not?

Mr. PICKENS. I think from the start, about 80-some odd years.

Senator JOHNSTON. Well, what this article says, it says the biggest paychecks—here are the amounts major Gulf shareholders would receive from Socal if the takeover is completed at the proposed $80 a share. And then it lists the Mesa Group—it describes you—the arbitragers, they would get——

Mr. PICKENS. How do they describe me?

Senator JOHNSTON. Excuse me.

Mr. PICKENS. How do they describe me?

Senator JOHNSTON. They do not even call you a predator. They just say your group. Then they say arbitragers would get $1,600 million, the Mellon Bank $775 million, State Street Research $213 million, First National Bank of Tulsa $145 million, College Retirement Equity Fund $137 million, Battery March, et cetera. Some of those I am sure are long-term stockholders.

Mr. PICKENS. Yes, sir. The one in Tulsa, the Warren family, they have been stockholders for 25 years.

Senator JOHNSTON. Well, these are hardly little people getting up in the billions of dollars and that is a third of the deal right there is going to 11 people, is it not?

Mr. PICKENS. Oh, no, that is not correct. You are talking about some of those funds there, Senator, at Battery March and State Street, those are pension funds. You are talking about thousands of people in each one of those accounts. Those are long-time holders of Gulf Oil. The short-term holders are going to be paying ordinary taxes on this.

Senator JOHNSTON. They are not little stockholders.

Mr. PICKENS. They are little stockholders. They are little stockholders. In the Mellon Bank, they have over 1,200 accounts in that.

Senator JOHNSTON. I understand that, but Mellon Bank is not a small stockholder of Gulf Oil.

Mr. PICKENS. They have many small stockholders in the Mellon Bank.

Senator JOHNSTON. I understand that. That is not what I asked you.

Mr. PICKENS. Well, Mellon Bank does not own any stock in Gulf Oil, I do not think. We do not see them as a stockholder. Those are trust accounts. There are over 1,200 of them in those accounts at Mellon Bank.

It is in Gulf's proxy material.

Senator JOHNSTON. The Mellon family.

Mr. PICKENS. That is what I am saying, 1,200 Mellons is the way those are broken down. [Laughter.]

The CHAIRMAN. Let us get quiet. Let us get quiet.

Senator JOHNSTON. You are a very wiley witness in addition to being a good entrepreneur. My point is and the point that the Wall Street Journal makes, which is a very valid point, and if we got to the bottom of all these answers and questions, we would find that, sure, there are some little stockholders. There are some little widow women and crippled people who are some of these stockholders.

Mr. PICKENS. Senator, I have files from small stockholders at Gulf Oil.

Senator JOHNSTON. I know you do. I am sure you got some good letters from them.

Mr. PICKENS. Excellent letters.

Senator JOHNSTON. But most of this money is going to some big time operators. They are going to make some good, red-blooded American profits and that is legal right today.

Mr. PICKENS. I think we can demonstrate to you that 75 percent of the holders of Gulf Oil will be long-term holders. And when I see that the speculators have moved in on this play, I do not believe it is near what has been described by some people. We will be glad to go through that analysis with you.

Senator JOHNSTON. Mr. Chairman, thank you very much.

The CHAIRMAN. Mr. Pickens, I notice you spoke about crippled people. You better be careful how you describe them that way. Mr. Watt had to leave office because he called people cripple.

Mr. PICKENS. Mr. Chairman, wait a minute. Just to correct the record, that Senator Johnston was the one that mentioned crippled people; I did not do that.

The CHAIRMAN. Oh, was that Senator Johnston?

Mr. PICKENS. Yes, it was. [Laughter.]

The CHAIRMAN. Oh, excuse me.

Mr. PICKENS. I did not use that word.

Senator JOHNSTON. I forgot that that is a bad word.

The CHAIRMAN. You had better call them handicapped. At any rate, we all have much sympathy for handicapped people.

Let me see now.

Senator Hatch.

Senator HATCH. Thank you, Mr. Chairman.

Mr. Pickens, it is my understanding that Senator Johnston's proposal applies to any transactions that are in the antitrust review process. Is that your understanding?

Mr. PICKENS. Yes.

CONCERN OF SHAREHOLDERS

Senator HATCH. If so, would such a retroactive application of law create hardships to the companies involved, their shareholders, the credit markets, Wall Street, and others?

Mr. PICKENS. I think it would be devastating to the oil industry.

Senator HATCH. Why would it be devastating to the oil industry, since it appears that just a few big companies are involved here?

Mr. PICKENS. I think that you would throw a cloud right over the industry. You know, Wall Street can stand good news and bad news. They cannot stand uncertainty.

Senator HATCH. What if we did not care about how much the industry suffered? How would it affect the country?

Mr. PICKENS. The country?

Senator HATCH. Yes.

Mr. PICKENS. Do we have to leave that other subject that quick, Senator Hatch?

Senator HATCH. Go back and say whatever you like.

Mr. PICKENS. I mean, if we do not care about what happens to the stockholders?

Senator HATCH. Apparently some do not.

Mr. PICKENS. Well, I agree with that. I agree with that fully, that some people do not care about the stockholders.

Senator HATCH. It seems to me everytime somebody comes out and says, well, "these great big oil companies," that is kind of a misnomer. There are a lot of little people who own stock. Some of them may be wealthy, but a lot of whom are not.

Mr. PICKENS. That is correct. I had a lady come up to me when I made a speech a week ago in Los Angeles. She came up after I got through and she said, Mr. Pickens, we appreciate very much what you are doing for us. I said, you must be a Gulf stockholder. She said, yes, I own 3,000 shares and it is my primary asset. So it does make you feel good when somebody comes up and says that to you.

Stockholders are the cornerstone of the free enterprise system, and if we remove that and put any doubt on that situation, we are not going to have that capital available to us in our capital markets. We cannot lose that credibility.

Senator HATCH. Well, there would be a general loss of confidence in the whole industry, would there not?

Mr. PICKENS. Absolutely; it would. To single out one industry and throw a cloud over it, I cannot believe that you are going to have that kind of legislation for one industry. If we are going to do that, let us get them all in.

Senator HATCH. Well, you are not only doing it for one industry. You are doing it in a selected period of time for certain companies in one industry, ignoring other mergers that have gone on before that have little or no more justification than these mergers do.

Mr. PICKENS. Well, you have the airline industry which is doing very well in a restructuring process. You have an oil industry that is trying to restructure itself to improve its image and be better and more efficient for the consumer. And we have everybody trying to stop all this process.

Senator HATCH. Well, does it not create two different classes of oil companies, the superlarge and those that may be everybody else if we have this kind of legislation?

Mr. PICKENS. If we have this kind of legislation, I do not see how this legislation is going to cause superlarge.

Senator HATCH. Well, remember there are a couple of mergers that will be ignored by this legislation because they picked right out of the air a certain period of time that just happens to cover these particular mergers.

Mr. PICKENS. I oppose this kind of legislation because I do not think it is in the best interest of the country, the consumer, or the stockholder.

Senator HATCH. Let me ask you this: Do you believe that the current wave of oil mergers presents any problem which must be addressed by Congress?

Mr. PICKENS. I do not. I do not see any reason to have any legislation of this type because of the mergers. I think it is a normal process in the free enterprise system and it should be allowed to proceed. The restructuring will be healthy for all concerned.

Senator HATCH. I have to admit I missed part of the testimony because we had to go to the White House, but—and I do not know what was said. But what was said before certainly did not lend a lot of credibility to the proposition that we need more scrutinous antitrust action. It did not lend a lot of credibility to those who feel that bigness is bad or that big mergers are bad without giving any consideration to the fact that they may be mergers of two big companies, but there are hundreds of thousands of people involved that could be injured and hurt by it.

Mr. PICKENS. So many times that these larger companies such as Socal-Gulf have more stockholders than small companies have. Somehow this is lost, the shareholders interest is lost.

Senator HATCH. Let me tell you, as a general rule, the Senator from Louisiana, I think, speaks very forthrightly and very knowledgeably about the oil industry. And I am having a rough time here because generally I like to listen to him and support him in the things that he feels deeply about, and I am concerned if there is some way that antitrust laws should apply differently here, I would like to have that pointed out by you or by anybody else.

If they do not apply differently here and the argument is that bigness is bad or that we do not have to be concerned about the dislocations to the marketplace, to the stockholders, to the pension funds, to all of the other interests in these matters, then I think that may be another matter.

If this bill is enacted by the Senate, would it interfere with the direct, free flow of capital in the marketplace, substituting Federal Government regulation and intervention for determining the most efficient allocation of capital?

Mr. PICKENS. Well, if this legislation was passed, you are going to damage the industry and the marketplace where they go for one

method for their financing. I mean, if you are talking about pulling billions of dollars out of an industry, you are going to do it right here with this kind of legislation. There is not going to be any interest in these stocks.

Senator HATCH. Your point is well taken. You seem to say, look, if you are going to do that, do not do that just for a few selected companies.

Mr. PICKENS. Oh, no. If we are going to do it, let us cover the waterfront if that is the way it has got to go.

Senator HATCH. As I have sat through these antitrust hearings through the years here on the Judiciary Committee, I found that the antitrust laws are pretty embracive. In other words, they really embrace almost every major problem that exists from an anticompetitive, monopolistic, or other type of price control or fixing process.

Mr. PICKENS. I have never had any experience with the antitrust laws because I have never been in that position before. But just as an outsider looking in on this one, I cannot see that there is any problem here because the industry is so fragmented. Even if you take the marketing and refining operation of these two companies, you are still talking about only 10 percent of total in the country. From my position it looks like we have adequate laws to take care of those situations in the antitrust area.

Senator HATCH. Well, thank you, Mr. Chairman. That is all I care to ask at this time.

The CHAIRMAN. Mr. Pickens, a corporation goes into business, of course, to make money. They have a right to do that, to make a profit. Stockholders invest in a company for the purpose of making a profit. And there has been a good deal said about stockholders and I can fully understand that and that has got to be respected. I want to ask you this question. If this merger goes through, is it in your opinion for the best interest of the general public?

And if so, how?

Mr. PICKENS. Absolutely.

The CHAIRMAN. How?

Mr. PICKENS. The consumer will see a more efficient operation of the combination of Socal-Gulf. Consequently, it could very well feed into the consumer's pocket. Second, the stockholder is going——

The CHAIRMAN. And then you think oil would be cheaper?

Mr. PICKENS. No, I do not think oil will be cheaper because the pricing of oil is away from us in the OPEC cartel, but I do see that there could be some efficiencies here that the consumer could realize.

Second, I see the stockholders are going to receive $13.2 billion.

The CHAIRMAN. I understand the stockholders from Gulf would gain by it. I am asking about the general public, the great masses, 250 million people in this country, and only 1 million or less would be affected here as stockholders. Now, what about the other 249 million people, how will they be affected?

Mr. PICKENS. Well, I will answer that but I would like to answer something first if I might. Those people are going to prosper by the $2 billion in taxes that will come into the general revenues of our country.

The CHAIRMAN. In other words, the capital gains the stockholders will pay from their increasing value of their stock by virtue of the sale?

Mr. PICKENS. Yes. On a pure company basis, Gulf Oil stock would sell something slightly under $40 a share. And here Socal has an offer on the table for $80 a share. So there are about 40 points in here. You can assume, I believe, with some accuracy that the Gulf stockholder's average price is probably $40 a share. Our cost is $45 a share. Ours is over the average price of the Gulf stockholder.

There are 40 points in here on 165 million shares. That is a profit of $6.6 billion. And that will be where the taxes will come from on that $6.6 billion. Now, we get nailed pretty good for how much we make out of this deal When you look at it, Mesa Petroleum comes out of the deal, pretax, about $500 million on an $80 deal. That is 8 percent, 8 percent of the $6.6 billion. I mean, it is very much in line with the real estate commissions.

The CHAIRMAN. Can you see any detriment to the general public if this merger goes through between Gulf and Socal?

Mr. PICKENS. Not at all.

The CHAIRMAN. You see no detriment whatever to the general public?

Mr. PICKENS. Absolutely not.

The CHAIRMAN. On the other hand, you feel it would be to the advantage of the general public.

Mr. PICKENS. I think it could be to their advantage, there certainly is no disadvantage to the general public.

The CHAIRMAN. Senator Hatch, do you have another question? Go ahead.

Senator HATCH. Well, let me just ask one other question. It is along the same line as the chairman's. Without the Johnston amendment, what terrible things do you think will happen in the next 6 months?

Mr. PICKENS. What terrible things?

Senator HATCH. If we do not enact this amendment.

Mr. PICKENS. If we do not enact.

Senator HATCH. Yes. If we do not.

Mr. PICKENS. And we just go ahead and proceed?

Senator HATCH. What are some of the terrible things that are going to happen? Some of our colleagues feel that some very terrible things are going to happen.

Mr. PICKENS. I think the industry is in a very healthy process of restructuring. I think it is good. I think the industry will be more acceptable to the consumer and to the American people. I think it will do a better job for its stockholders. I think we are on the right track.

Senator HATCH. So, you do not think that there will be terrible things happening if this legislation does not pass and this one merger is allowed to go through?

Mr. PICKENS. I think that anything that would happen would be good.

The CHAIRMAN. Mr. Pickens, some people feel if these mergers go through with oil companies, there will be some other businesses that will follow suit and you will end up with just a few big oil

companies and maybe a few big grocery concerns or a few big other concerns in the country. How do you feel about that?

Mr. PICKENS. That does not particularly bother me because I feel like that is the free enterprise system and that is America. I do not think you can be stepping in and saying this deal can go and this one cannot go. I think that as the stockholders become more and more aware—and I promise you, we are helping a little bit in that—that the stockholders are becoming more aware of what is going on. Consequently I think you will see there is going to be more pressure put on these managements. You should never take rights away from the stockholders because that is where the funding comes from for these companies.

And so we have got to leave that intact and not tamper with it. Consequently the stockholders, as they become more and more informed, are going to put pressure on managements to do a good job.

The CHAIRMAN. Is it better to have a few big oil companies or a few big other companies or have a lot of little companies? Which is to the best interest of the general public?

Mr. PICKENS. I think when I look back over the industry, of course, the largest being Exxon, substantially larger than the next largest, Mobil, Socal, Gulf, and on down the line; Texaco I think is in there No. 3. When I look at it, I am not fearful of the sizes of those companies. As a smaller company, we are the 92d largest oil company in the United States, I believe. We have no problem competing with these people. We feel very comfortable. We have our pluses and we can do things better than they can in some areas. They can do things better than we can in some areas. It is just good, healthy competition.

So I do not get concerned about oil companies getting larger. And that does not particularly bother me. I think that if I was running a major oil company, I would consider downsizing at times if I thought it was in the best interest of my stockholders. But I have not been in step with the major oil companies' CEO's for a long time, about 33 years, in fact.

The CHAIRMAN. From your testimony, I would assume that you do not favor any changes in the antitrust laws.

Mr. PICKENS. I think that the general public is well protected by the antitrust laws.

The CHAIRMAN. All right. Senator Johnston, do you have any more questions?

Senator JOHNSTON. No, Mr. Chairman.

The CHAIRMAN. Mr. Pickens, thank you very much for your presence here. We appreciate your testimony.

Mr. PICKENS. Thank you.

The CHAIRMAN. Now, Mr. William P. Tavoulareas, president of Mobil Corp. Mr. Tavoulareas, come around and have a seat.

Mr. Tavoulareas, do you have a written statement?

Mr. TAVOULAREAS. Yes.

The CHAIRMAN. Would you like for that to be put into the record in full?

Mr. TAVOULAREAS. I would.

The CHAIRMAN. And then would you care to make a résumé or do you just want to go to questions?

Mr. TAVOULAREAS. I would much rather make a résumé if I may.
The CHAIRMAN. All right. You may proceed.

STATEMENT OF WILLIAM P. TAVOULAREAS, PRESIDENT, MOBIL CORP., NEW YORK, NY

Mr. TAVOULAREAS. My name is William P. Tavoulareas. I am president of Mobil Corp. My purpose in appearing before you today is twofold; one, to urge you not to adopt any moratorium; and two, to point out why such legislation, if passed, should not be retroactive and not in any event be applied to the transaction of Mobil-Superior.

In recent weeks there has been a good bit of activity involving the stocks of oil companies. The phenomenon we are seeing in large part reflects the fact that the stock market for various reasons undervalues the reserves of these companies in relation to the real cost of replacing them.

As a consequence, there is an incentive to purchase these reserves when they become available on the market. But this is not true only of oil. It is also true of other resources. I am sure we all have noted the activity that has begun in the forest products industry and minerals. The same thing is and will happen in any industry or company if the current stock market price consistently undervalues the company.

The stock market does not usually reflect what I believe is the true or replacement cost value of natural resources. Until this phenomenon in the stock market values adjusts, if ever, there will be an incentive for legitimate purchasers to buy and for sellers to sell. There will also be an incentive for entrepreneurial types, sometimes called raiders, to try to capitalize on this situation by creating a take over atmosphere in respect to a particular company and then profiting on the stock they have previously purchased.

It also provides a tremendous incentive to those specialists in leveraged buy outs who bring nothing to the target company but the hope of financing their acquisitions with the target assets.

It will not surprise you to hear me say I believe any moratorium legislation is unwise for this country. I believe that history consistently teaches that the free market is a wiser, more efficient allocator of capital than is government. Even if one does not accept this view, it is illogical to apply any moratorium legislation only to the petroleum industry. It is furthermore unfair and disruptive to make any such legislation retroactive. Business must be able to proceed on the assumption that at least the rules will not be changed retroactively.

Nothing is more likely to destroy the confidence in our market system. Any legislation that prohibits the shareholder from selling to certain potential buyers is an infringement on a free market and will eventually hurt all shareholders.

Further, the Superior-Mobil transaction is different. Whatever may be the wisdom of adopting legislation to inhibit hostile takeovers or takeovers which are financed with target assets, it would be unwise and would set a very dangerous precedent to bar transactions initiated and supported by willing sellers.

The transaction between Mobil and Superior is precisely such a transaction. Certain of the major shareholders of Superior and the company itself invited Mobil to make a bid. These shareholders, who are descendants of the founder, had already decided to sell before we had any contact with them. There is no element of hostile takeover involved in this case. There is a very important principle at stake here, the free choice of shareholders to decide they want to sell and their ability freely to choose a buyer to make the purchase.

There has been much talk about stopping big oil. In this regard, if the principle shareholders and the board of a company like Superior voluntarily decide to sell, is Superior in better hands with Mobil or with a corporate raider or with a leveraged buy out concern?

The answer is clearly Mobil because the size and nature of the transaction will not put any inordinate strain on Mobil. Hence, the chances are best that the business will survive. Mobil's own earnings are sufficient to support the programs of Superior. If a corporate raider acquired the stock, we would see royalty trusts and spinoffs. If a leveraged buy out concern purchased the company, we would probably see partial or total liquidation, since such concerns would not have the financial strength of Mobil to support Superior.

Once a seller decides to dispose of his stock, it is better that acquisitions are made by financially sound buyers. If concentration is a threat, the antitrust laws will protect the consumer. Let me draw your attention to certain other aspects of the Mobil-Superior transaction which make it unnecessary or undesirable for Congress to interfere.

All of the shareholders of Superior will have the opportunity to sell their shares at substantially the same price. Both the board and management of Superior support the transaction. Some of the principal beneficiaries of this transaction are educational or charitable institutions including the University of Southern California, Stanford, Pomona College, and Occidental College. They stand to receive over half a billion dollars as a result of these transactions.

Superior has no manufacturing and marketing operations. Therefore, there are none of the antitrust problems associated with such operations. Nor are there any problems of concentration. Superior produces less than 1 percent of America's total oil and gas. Mobil produces less than 3 percent. Nor would the merger significantly increase Mobil's size. The acquisition of Superior would add only about 3 percent to our gross revenues.

The total value of the Mobil-Superior transaction at $5.7 billion is considerably smaller than some other recent transactions. Furthermore, the $45 price per share is only slightly higher than the current market price.

One of the most persistent concerns voiced about these transactions is their effect on our financial markets. I do not believe such concerns are justified. This is particularly true of the Mobil-Superior transaction. First, a large portion of the purchase price will be paid with new Mobil debt. This will have virtually no effect on the credit capacity of our financial institutions.

Second, a substantial portion of the purchase price will be returned immediately to the banking system. Nearly 60 percent of

the shares of Superior are held by institutions or large shareholders who should probably return the funds to the capital markets.

Third, much of the cash will be provided by foreign banks funding themselves in the Eurodollar market. This will further reduce the effect on domestic bank liquidity. In this connection, I commend to you the conclusions of the Securities and Exchange Commission Advisory Committee on Tender Offers announced last July. Based on an extensive study in consultation with the Federal Reserve Board, they concluded that there is no material adverse effect on the credit markets resulting from control acquisition transactions.

You will want to keep in mind that transactions of this kind will generate substantial revenue for the U.S. Treasury in the form of income taxes, although the exact amount will vary for individual shareholders.

Let me make one other very important point. Questions have been raised about our willingness to expend funds to find and develop domestic oil and gas after we have made this acquisition. Exploration and development in the United States has always enjoyed top priority in Mobil's investment decisions. Assuming attractive opportunities are available in the future, this will continue to be true. I can promise you that.

Now, let me summarize. While I understand some of the concerns behind some of the legislation, one, I do not believe the legislation I have seen proposed will benefit the industry, the country, or the consumer. Most of all, it is unfair to the average shareholder.

Two, it will interfere with a free market and discourage people from investing in oil when our country should be encouraging such investments.

Three, if a moratorium is enacted, why should it not apply across the board and not only to oil? If a moratorium is enacted, it should not be retroactive in effect. People must be allowed to enter into business transactions on the basis of the law existing at the time without the fear that Congress may retroactively nullify a deal.

If there is legislation or a moratorium, let it be directed at the corporate raider or the leveraged buy out takeover. It should not inhibit transactions voluntarily initiated by the stockholders and management of a company being sold.

I would like now just to comment very briefly on some of the principles that I have heard expressed here. First of all, people said all we are asking you to do is wait 6 months as if we have an option on shares. We have no option. If we wait 6 months, there may be no deal. We have heard people play with the tax effect of these transactions and criticize companies who would take interest on the loans as a deduction and then say the banks who receive the interest do not pay much taxes. It is an illustration to me that some people do not understand what happens. The banks do not keep the interest; it is the depositors or the people who give money to the banks that make the interest. The banks make a very small markup, and the people that receive the interest will pay the tax, just like the fellow who deducts the interest will get a deduction.

Some of the economic theories I heard today or the theories of OPEC—and I have been in this business for 37 years—I would not

even recognize. And I wish I would have more time with the people involved to discuss them.

Now, what we have in the oil industry going on today is a readjustment in the structure and a readjustment in the structure—and the competition is not only ourselves; the competition is foreign. The competition is OPEC. And we have no monopoly on the oil industry worldwide. The stronger we make an industry in the United States, the more oil we can explore for and produce, the more we can explore for and produce abroad, the more we will keep ourselves independent from foreign domination.

That is all I have to say. Thank you.

The CHAIRMAN. Thank you very much. Mr. Tavoulareas, I want to ask you this question, similar to the one I asked the other officials. What detriment do you see of the merger between Mobil and Superior?

Mr. TAVOULAREAS. No detriment at all. Only a benefit.

The CHAIRMAN. If this merger goes through between Mobil and Superior, do you visualize that that is going to affect the consumers of oil in this country?

Mr. TAVOULAREAS. Well, I hope—I cannot guarantee that. I hope as a—what we have here is a company like Mobil who has done well in exploration over the past 15 to 20 years, but we are basically a crude short company in the United States. What we have in Superior is a very efficient explorer. But for one reason or another, there has been a big difference of opinion as to how that company should be operated between the major shareholders, among the major shareholders, and the management.

That whole group has now agreed they would be better off selling out to us. They think it would be better off for them and better off for the company. They think it is their best chance to survive. If Superior survives, then I know that is the best chance to continue to find and explore for oil. To that extent, that will be better for the consumer.

The CHAIRMAN. So from the standpoint of the general public, you do not see any detriment on account of this merger. Do you see any benefits to the general public?

Mr. TAVOULAREAS. Yes. As I said, I think to the extent that we are combining two fairly efficient exploration operations, the amount of money involved is not going to put a strain on our organization, organization like ours that is worth $35 billion, has budgets between $3.5 billion and $5 billion, makes $1.5 to $2 billion a year, and we absorb Superior who had a $1 billion expenditure. I think if anything we can supplement their budgets.

The CHAIRMAN. The distinguished Senator from Utah.

Senator HATCH. Mr. Tavoulareas, when shareholders have decided to sell a company, as I understand is the case with Superior, will the company be better off merged with another responsible company or by sale to a corporate raider or perhaps sale via the leveraged buy out approach?

Mr. TAVOULAREAS. I am sorry, Senator. I will repeat what I said. I said there are really three buyers today in the marketplace. One I do not call a buyer. He is a corporate raider, moves in, senses a situation of chaos, drives the price up and he really does not want to take over. He drives the price up and gets out.

The second, we have a leveraged buy out type situation where the fellow wants to use the assets of the corporation in order to finance the transaction. Well, that really means you have a very tight financial situation.

And the third is the financially sound organization that can use its own credit as well as the assets they are purchasing. Clearly, of those three types of buyers, which are the only buyers in the marketplace, the best chance of survival comes with the last. The other two are liquidators of a sort.

Senator HATCH. What impact will these mergers have on concentration in the oil industry? And I am talking about the merger of Mobil and Superior and to your knowledge, if you can, the merger of Socal and Gulf.

Mr. TAVOULAREAS. Very, very minor. We have two different businesses in the United States. We have no refining and marketing which is where almost all of the attention in the past on antitrust has been given with little or no attention to producing because it did not need any attention.

Anybody can get into the producing business or the exploration business. At one time there were more than 4000 companies in that business. So in our case, for example, we are less than 3 percent of U. S. production and they are less than 1 percent of U. S. production. Beyond that, two-thirds of what we are purchasing is gas and we are still short oil. So we have a real appetite to look for oil.

I would say the same comment on Gulf and Socal. I would imagine together they are no more than 5 or 6 percent, which is still a very small part of the market, on the producing side. And they will settle their refining-marketing side with the Justice Department or the FTC.

IMPOSED HARDSHIPS

Senator HATCH. What hardships would be imposed on the merging companies by this legislation—hardships on the companies, their shareholders, credit markets, Wall Street and others—by the retroactive application of the laws proposed by the so-called Johnston amendment?

Mr. TAVOULAREAS. I think if you ever have anymore hearings, I would recommend that you call some of the investment bankers, some of the commercial bankers, to give you some reactions to that. I have spoken to them in the last few days. They say this will put an absolute lid on investments in the oil industry, and Wall Street would worry that it would carry over to other industries, because some of these raiders will move their actions over to other resource companies, who have the same phenomenon—low values, because they are long-term-type companies. That is one effect.

The retroactive effect, they think is an absolute disaster. You can imagine a fellow on Wall Street, sitting in a room, making that deal, making this deal, making that deal, and all of a sudden, he has made all the deals, and he has been told, "You have got all the deals. You are stuck.

"Well, I will tell you what. We are going to make you give it away."

Just imagine, for example, if Texaco bought 11 billion dollars' worth of stock, and it was told it could no longer own 11 billion dollars' worth of stock. Imagine what would happen to the Gulf shareholders who think they have $80. These are a lot of little shareholders. We have 260,000 shareholders in our company. I am not sure how many Superior has. This is not us. This is not me. We are just corporate management. We are a lot of shareholders, 260,000. And to be suddenly told that instead of getting $45—and here, the Kecks and the Day families, they founded this company, and there are some charities in there—and to finally decide after many years they want to sell it. They will be told: "You cannot sell it to the highest bidder. You will have to wait 6 months. I do not know what is going to happen."

Senator HATCH. What compounds it is that they not only say you cannot sell it to the highest bidder, but they seem to trump up a phony antitrust case to justify the retroactive application. I have yet to hear——

Mr. TAVOULAREAS. I have been speaking to these Senators for the last couple of days. I just say to them, I want to know why you are putting Mobil-Superior into this box, because we do not have any antitrust problems.

Senator HATCH. Well, as I understand it, in your particular case, I do not know of anybody who has accused you of having any antitrust problems in the Mobil-Superior deal.

Now, it is admittedly a large transaction. But you know, the antitrust laws are very restrictive, they are very strong, they do a tremendous job of protecting the public. But do you know of any antitrust implications in the Mobil-Superior transaction?

Mr. TAVOULAREAS. No, none. They may ask us to continue to sell Superior Oil to the people who are buying Superior Oil, and we would readily agree to that.

Senator HATCH. I think for those who do not understand it, if Superior is owned in part by a large family holding, that family really cannot place their shares on the marketplace unless they go through a complete registration to do so, or unless they can sell to somebody like you.

Am I wrong or right on that?

Mr TAVOULAREAS. Well, they know if they tried to sell 22, 23 percent in the market, they would never realize $45 a share.

Senator HATCH. Well, it would just drop.

Mr. TAVOULAREAS. The price would nosedive.

Senator HATCH. Oh, there is no question.

Well, do you believe that the current wave of oil mergers presents any problem that we really should address here in Congress? I think that is an important question.

Mr. TAVOULAREAS. I honestly—if you want to have some targets and yardsticks on the refining and marketing side, I guess there ought to be some yardsticks on the producing side. But we are so far from any meaningful yardstick. Furthermore, the producing side is so different. And what is critical about the refining and marketing is we want to be sure there is competition so people bid against each other on prices. In a producing field, there is almost none of us who own a producing field fully; we already are together

in producing fields. We operate our own share of the producing fields.

Senator HATCH. Sometimes you operate jointly, I suppose.

Mr. TAVOULAREAS. Right. We may operate jointly, but we take care of our own oil. So I just do not see any problem on the producing side at all, at the levels we are talking about, and even much higher levels.

Senator HATCH. Well, without this amendment—I will ask you the same question I have asked Mr. Pickens—without this amendment, what terrible things do you think would happen in the next 6 months?

Mr. TAVOULAREAS. Nothing.

Senator HATCH. Well, with the amendment, do you think any terrible things would happen?

Mr. TAVOULAREAS. Yes, I said what I thought. First of all, you would be creating unbelievable chaos for some shareholders who think they have some money, and then you would have a lot of people who would say, "I am going to pull my money out of the oil industry," so you would adversely affect all oil stocks; and you would hurt an industry that everyone here seems to think they want to help. They say, "The reason I am worried is because I am worried about the exploration levels." If people will not let them go through with this, you will not have to worry about the exploration levels, because people will not be putting money in the industry.

Senator HATCH. So, people who are arguing that this type of a statutory approach will lend credibility or even impetus to more exploration expenditure, are really arguing the wrong thing.

Mr. TAVOULAREAS. I said it in my speech, and I will say it again. We spend money all around the world. We spend the major part of our money on exploration and producing, and we spend the major part of that in the United States. It is first priority with us. The only problem we have is that we have the opportunities, and that will continue to be first priority.

Senator HATCH. Well, thank you, Mr. Tavoulareas. We are happy to have you testify before the committee today.

Mr. TAVOULAREAS. Thank you.

Senator HATCH. The last panel includes Mr. Phillip R. Chisholm, who is the executive vice president of the National Oil Jobbers Council of Washington, DC; Mr. Victor Rasheed, executive director of the Service Station Dealers of America, Washington, DC; Mr. Edwin Rothschild, assistant director of the Citizens/Labor Energy Coalition of Washington, DC, and Mr. Joseph C. Story, senior economist for Middle East Services, Wharton Econometric Forecasting Associates, also from Washington, DC.

We will begin with you first, Mr. Chisholm.

STATEMENT OF A PANEL, INCLUDING PHILLIP R. CHISHOLM, EXECUTIVE VICE PRESIDENT, NATIONAL OIL JOBBERS COUNCIL, WASHINGTON, DC; VICTOR RASHEED, EXECUTIVE DIRECTOR, SERVICE STATION DEALERS OF AMERICA, WASHINGTON, DC; EDWIN ROTHSCHILD, ASSISTANT DIRECTOR, CITIZENS/LABOR ENERGY COALITION, WASHINGTON, DC; AND JOSEPH C. STORY, SENIOR ECONOMIST FOR MIDDLE EAST SERVICES, WHARTON ECONOMETRIC FORECASTING ASSOCIATES, WASHINGTON, DC

Mr. CHISHOLM. Thank you, Senator Hatch.

My name is Phil Chisholm. I am the executive vice president of the National Oil Jobbers Council. We represent some 11,000 independent small business petroleum product marketers who are obviously very, very concerned about the wave of recent mergers. We appreciate the opportunity to appear before the committee today, and in the interest of time, I will touch briefly on two major concerns which we have with the merger.

Senator HATCH. If you would, please. We will put all of your prepared statements in the record, and if you can complete in 5 minutes, I would personally appreciate it.

Thank you.

Mr. CHISHOLM. Thank you.

The first major concern is the impact on competition. Much of the discussion today has focused on the impact of competition in crude oil and what happens with crude oil reserves. I, instead, would like to focus a little bit on downstream marketing, which we represent.

We see an immediate concern the impact these mergers will have on downstream marketing. We believe that downstream marketing is perhaps the most competitive aspect in the entire petroleum industry. The FTC, as evidenced by the proposed consent order in the Texaco-Getty merger, appears only to focus on the competitive concerns created by the horizontal market overlap between the two companies. The remedy of company spinoffs of downstream marketings may solve the immediate problems posed by horizontal overlap. However, this remedy fails to take into consideration the continuing viability of divested downstream operations. Particularly in the oil industry, the vested units are often franchisees which are protected under other laws, such as the Petroleum Marketing Practices Act.

Divestiture without consideration of the interests, competitive viability and legal protections of these small business franchisees harms them by depriving them of their source of supply and services. These shortsighted spinoffs may, in fact, create even greater competitive problems, for if these divested units sink and die after spinoff, their demise could lead to just the kind of anticompetitive situation which the antitrust laws and the FTC and Department of Justice guidelines are designed to prevent.

Moreover, we are afraid that some of the companies may be playing "briar rabbit" when they are ordered to sell downstream marketing operations. In the Texaco-Getty example, many of the properties Texaco is being told to sell off in the Midwest are in areas in which Texaco has long since withdrawn and is no longer serving. In the proposed Gulf-Socal merger, Socal may be more than willing

to sell off even more of the Gulf's refining and marketing facilities than even the FTC may require.

In essence, the competitive impacts of these mergers with the anticipated spinoffs are threefold. First, the markets served by the company being acquired loses a major competitor. Any new company which may acquire those spinoff facilities is likely not to be as strong a competitor as the company it replaced, unless it, too, is a major integrated company.

Second, the other major integrated companies still in the spinoff markets are in a much stronger position. They have seen a major competitor sell to a third party which likely will not be as strong a competitor as either of the two companies involved in the merger.

Finally, the acquiring company has greatly enhanced its position in the market because it has greatly increased its crude oil reserves at a fraction of the cost of new exploration and production and has been ordered by the Government to sell off what are generally considered the most unprofitable aspects of the acquired company.

The bottom line in such an analysis is that the major integrated companies tremendously enhance their posture in the market, while virtually every independent competitor is hurt. Some people may be very comfortable with the consequences of these actions. The National Oil Jobbers Council is not.

We have long questioned the efficiencies of integration in the petroleum industry. We believe, we have alleged, and we continue to believe that upstream crude oil profits have subsidized downstream markets, and we think those subsidies continue to exist.

With these mergers, however, fewer and fewer companies will be in a position to provide such marketing subsidies, thus putting those few companies which still can in a posture to take over any major retail markets which they desire.

The second major point I would like to address Senator, which goes directly to the focus of the legislation and to the focus of some of the questions you have raised, about what happens in 6 months if this legislation is not enacted.

We are very, very concerned about other potential companies that may be taken over and what that does to downstream marketing—the mention of Union, the mention of Kerr-McGee, the mention of Phillips, and what effects that will have on downstream marketing—and we think there needs to be some still picture, if you will, some type of freeze, until the full consequences can be evaluated of what is taking place.

Senator HATCH. But if the other side is right, that it will dislocate the stock market and cause a loss of confidence in the oil industry, that could really affect every one of your jobbers.

Mr. CHISHOLM. I think it could, but I think we are more fearful of what the consequences are if no action is taken. And I think many of the jobbers we represent are very concerned. I know the Getty jobbers who are in the areas Texaco must divest are very, very concerned. I know many of the other jobbers that would be affected by the Gulf-Socal merger are very, very concerned about their future, because whoever takes over those properties is not going to be—or, they do not believe they will be—nearly as competitively viable as

Gulf is, as Getty was, and they do not think the combination will improve the situation.

My time is up, and I will answer any other questions.

Senator HATCH. Thank you, Mr. Chisholm. We appreciate your testimony.

[The following was received for the record:]

STATEMENT OF

PHILLIP R. CHISHOLM

ON BEHALF OF THE

NATIONAL OIL JOBBERS COUNCIL

PREFACE

The National Oil Jobbers Council is a federation of 42 state and regional trade associations representing thousands of independent small business petroleum marketers. Members include gasoline and diesel fuel wholesalers, commissioned distributors of gasoline, gasoline reseller-retailers and a large number of retail fuel oil dealers. Members also wholesale or retail many other petroleum products, including kerosene, LP gas, aviation fuels and motor oils as well as residual fuel oil. Together our members market approximately 50 percent of the gasoline and 85 percent of the home heating oils sold in America under either their own private brand or the trademark of their supplier.

Mr. Chairman and members of the Committee my name is Phillip R. Chisholm. I am Executive Vice President of the National Oil Jobbers Council (NOJC). NOJC is a federation of 42 state and regional associations which represents some 11,000 independent, small business petroleum products marketers. Collectively these companies sell nearly 50 percent of the motor gasoline and 85 percent of the home heating oil marketed in the United States each year.

We sincerely appreciate this opportunity to appear before the Committee and express our concerns about the recent wave of mergers among the major oil companies. We do indeed have some serious concerns with these "mega-mergers" and we believe they raise a number of questions, questions which have yet to be satisfactorily answered. Our concerns center around several areas and I would like to touch briefly on just a few of those areas.

IMPACT ON COMPETITION

Perhaps our first and foremost concern is the potential impact such mergers will have on long-term competition within the petroleum industry and upon the independent petroleum marketers represented by the National Oil Jobbers Council. In our view, competition at virtually every level of the industry is clearly threatened by the oil industry mergers. Our most immediate concern, however, is the impact these mergers will have on downstream marketing, the segment of the industry in which our members are most involved, and the segment which we believe to be one of the most competitive in the entire petroleum industry.

The FTC, as evidenced by the proposed consent order in the Texaco-Getty merger, appears to focus only on the competitive concerns created by the horizontal market overlaps between the two companies. The remedy of company spin-off of downstream marketing operations may solve the immediate problems

posed by these horizontal overlaps. However, this remedy fails to take into consideration the continuing viability of divested downstream operations. Particularly in the oil industry, the divested units are often franchisees which are protected by other laws, the Petroleum Marketing Practices Act, for example. Divestiture without consideration of the interests, competitive viability and legal protections of these small business franchisees harms them by depriving them of their source of supply and services. These negligent spin-offs may in fact create even greater competitive problems, for if these divested units sink and die after spin-off, their demise could lead to just the kind of anticompetitive situation which the antitrust laws and the FTC and Department of Justice guidelines are designed to prevent.

Moreover, the acquiring companies are playing "briar rabbit" when they are "ordered" to sell downstream marketing operations. In the Texaco-Getty example, many of the properties Texaco is being told to sell off in the midwest are in areas from which Texaco had long since withdrawn and is no longer serving. In the proposed Socal-Gulf merger, Socal would probably be willing to sell off even more of Gulf's refining and marketing facilities than even the FTC may require.

In essence, the competitive impacts of these mergers with the anticipated spin-offs are three-fold. First, the markets served by the company being acquired (i.e. Gulf or Getty) loses a major competitor. Any new company which may acquire those spin-off facilities is likely not to be as strong a competitor as the company it replaced, unless it too is a major integrated company.

Secondly, the other major integrated companies still in the spin-off markets are in a much stronger position. They have seen a major competitor sell to a third party which likely will not be as strong a competitor as either of the two companies involved in the merger.

Finally, the acquiring company (i.e. Texaco or Socal) has greatly enhanced its position in the market because it has greatly increased its crude oil reserves at a fraction of the cost of new exploration and production and has been ordered by the government to sell off what are generally considered the most unprofitable aspects of the acquired company.

The bottom line in such an analysis is that the major integrated companies tremendously enhance their posture in the market while virtually every independent competitor is hurt. Some people may be comfortable with the consequences of that situation. The National Oil Jobbers Council is not.

Mr. Chairman, please do not misunderstand our posture. We have long questioned the efficiencies of integration, particularly as applied to downstream marketing. We continue to believe that independent marketers are the most efficient marketers in the gasoline business. That functional efficiency, however, is rendered irrelevant if a major integrated company uses upstream crude oil profits to subsidize its downstream markets. We have alleged previously and we still believe that such subsidies exist.

With these mergers, however, fewer and fewer companies will be in a position to provide such marketing subsidies thus putting those few companies which can in a posture to take over any major markets they desire. Critics of the oil industry have for years talked of "The Seven Sisters" and the power they wield in the industry. If the mergers continue will there one day be only three or four "sisters", or perhaps two? What effect would that have on competition?

Allowing these mergers could provide the clarion call for a major legislative restructuring of the petroleum industry such as crude oil divestiture.

IMPACT ON EXPLORATION AND DEVELOPMENT OF NEW RESOURCES

NOJC is also concerned that mergers involving billions of dollars cannot help but have a negative impact on exploration and production of new domestic oil resources. The Texaco-Getty, Socal-Gulf and Mobil-Superior proposed mergers would involve an expenditure of nearly $30 billion and yet would not result in a single new barrel of oil. In testimony before Congress a few years ago, one of the Hunt brothers reportedly made the observation that "A

billion dollars isn't what it used to be." There may be some validity to that observation, but common sense would seem to dictate that when a company, no matter how large, spends billions of dollars to acquire the existing reserves of another company, the incentive for the acquiring company to invest additional capital in possible risky new exploration activity is diminished.

As the incentive to drill for new domestic reserves is reduced by these mergers, the dependence on unstable foreign supplies is sure to be increased. This has a negative impact on the United States' balance of payments, as well as threatening the country's national security.

THREAT OF MORE MERGERS

Any of the announced mergers, if examined separately from the others, may not raise as many questions and concerns. It would be almost akin to examining a single piece of a puzzle. Only when that piece is combined with other pieces does the true picture emerge. Thus, it is with the mergers. Three major mergers have been announced within the last 60 days. Wall Street analysts are already speculating on the companies which might be the next takeover target, and at least half a dozen companies are on that list. The mere threat of being taken over can lead a company to take actions which may not be in its own long-term best interests. The March 19 issue of Business Week magazine made the following observation: "Oil companies are under intense pressure to survive by getting bigger through acquisitions and uglier with debt -- even though the rising leverage raises risks."

OTHER IMPACTS

There are a whole range of other factors to consider as part of these mergers. For example, what are the consequences of the merger on revenue to the federal government? Socal will be able to write off from its federal taxes the interest paid on the money borrowed to finance the acquisition. In addition, it will be able to depreciate and amortize the assets acquired from Gulf. Does the capital gains taxes paid by Gulf shareholders come close to offsetting that loss to the federal treasury?

What are the impacts on energy resources other than oil or gas? What do these mergers do in terms of combining other energy resources such as coal and nuclear energy?

What do these mergers mean in terms of unemployment?

What ramifications will these mergers have on small business competitive franchisee customers of the acquired company?

What are the impacts of the mergers on the state and local economies in those areas directly affected?

These are questions we cannot answer, but which we believe need to be addressed prior to any final approval of the mergers.

SUMMARY

This country has enjoyed a period of relative energy stability over the past few years, but that very stability may have led us to drop our guard somewhat. It would behoove us to remember that today's so-called "glut" can suddenly and unexpectedly become tomorrow's shortage. The recent trend to acquire oil reserves via mergers and acquisitions does not bode well for competition within the oil industry, for new exploration and development, for American consumers or for our national security.

The federal government stands to lose as well, as millions upon millions of dollars in interest and amortization costs are written off by the acquiring companies.

Perhaps the thing to keep foremost in mind is that despite the tens of billions of dollars being spent on the mergers, despite the potential threat these mega-mergers pose to competition and to national security, and despite all the other possible consequences associated with the mergers, not a single barrel of new oil will have been added to our reserve base.

At the very least Mr. Chairman and members of the Committee, these gigantic mergers, as well as hostile takeovers, should be put on hold until some of the many questions surrounding them can be answered. The National Oil Jobbers Council strongly supports the pending proposal which calls for a six-month moratorium on mergers of the nation's 50 largest oil companies. We also believe that the FTC and Department of Justice Merger Guidelines must be expanded to include consideration of the effects on small business franchsees of merger approval mechanisms such as divestiture. Currently these Guidelines are written so as to effectively preclude appropriate review of these downstream effects.

Again, Mr. Chairman and members of the Committee, thank you for allowing us to be here today. I will gladly answer any questions you may have.

MEMBERS OF THE NATIONAL OIL JOBBERS COUNCIL

NOJC represents these member associations:

Alabama Oilmen's Association
Arizona Oil Marketers Association
Arkansas Oil Marketers Association, Inc.
California Independent Oil Marketers Association
Colorado Petroleum Marketers Association
Independent Connecticut Petroleum Association
Florida Petroleum Marketers Association
Georgia Oilmen's Association
Idaho Oil Marketers Association
Illinois Petroleum Marketers Association
Indiana Oil Marketers Association, Inc.
Intermountain Oil Marketers Association
Petroleum Marketers of Iowa
Kansas Oil Marketers Association
Kentucky Petroleum Marketers Association
Louisiana Oil Marketers Association
Maine Oil Dealers Association
Michigan Petroleum Association
Mid-Atlantic Petroleum Distributors Association,Inc.
Mississippi Petroleum Marketers Association
Missouri Oil Jobbers Association
Montana Chapter, Intermountain Oil Marketers Association
Nebraska Petroleum Marketers, Inc.
Independent Oilmen's Association of New England
Fuel Merchants Association of New Jersey
New Mexico Petroleum Marketers
Empire State Petroleum Association
North Carolina Oil Jobbers Association
Northwest Petroleum Association
Ohio Petroleum Marketers Association
Oklahoma Oil Marketers Association
Oregon Oil Jobbers Association
Pennsylvania Petroleum Association,Inc.
South Carolina Oil Jobbers Association
South Dakota Petroleum Marketers Association
Tennessee Oil Marketers Association
Texas Oil Marketers Association
Virginia Petroleum Jobbers Association
Washington Oil Marketers Association
West Virginia Oil Jobbers-Distributors Association
Oil Jobbers of Wisconsin, Inc.
Wyoming Petroleum Marketers Association

National Oil Jobbers Council
1707 H Street, N.W.
Washington, D.C. 20006

(202) 331-1198

Senator HATCH. Mr. Rasheed.

Mr. RASHEED. Thank you, Senator Hatch.

My name is Vic Rasheed. I am executive director of the Service Station Dealers of America.

We have one concern with the mergers, primarily one concern. That is that it will lead to eventual control of the retail market by the major oil companies.

Our concern with an amalgamation of these major refiners is its effects primarily on the price that motorists may have to pay for gas in the future, but more so, we are concerned about the fate of thousands of retail marketers across the country. Will they remain as efficient competitive outlets, able to sell branded product with all related services to millions of motorists who depend upon them, or will they be sold for their real estate value, in a quick grab for profit? Or, will they be traded around——

Senator HATCH. Mr. Rasheed, just on that point, the present antitrust laws do protect against all aspects of market dislocation and what you are talking about here. The FTC has to look into every aspect of that. Just because these people want to merge does not mean that they do not have to meet the criteria of the antitrust laws. I just wanted to point that out to you.

Mr. RASHEED. Well, I understand that, and in a second, I will refer to that again, Senator Hatch. But these are our concerns.

Senator HATCH. OK.

Mr. RASHEED. Will they be traded like baseball cards? Will our domestic gasoline industry become a chain of company-operated, automated, unattended, ghost stations, as we already have seen in Europe?

We have studied the FTC consent order and the Texaco-Getty merger. Nowhere in that 60-page document is there any mention of how the disposition of some 1,900 retail outlets will affect the business interests of the independent marketers, and we are talking about dealers and jobbers; or, how the services which they provide to their customers will be protected.

Rather, the disposition of stations is referred to in a manner similar to making transactions on a monopoly board. These are not pieces of plastic; these are independent businesses, with real, live people. Businessmen, who have spent a lifetime serving their communities, at the very least deserve the right to purchase their locations which the companies must divest.

Instead, we see 600 branded Getty dealers in the Northeast being turned over to a small, nondescript, unbranded, independent marketer, Power Test, which is being loaned the money to purchase them by Texaco. Many of these dealers are frustrated at being abandoned by Getty and outraged by Texaco's callous disregard of their interests.

In the near future, we will be filing comments with the FTC, suggesting that the Texaco-Getty consent decree should include some additional provisions to protect the small businessman and consumers.

This may be the case of trying to lock the barn door after the horse is out. However, these points should be considered in the event of future mergers.

I will not read the points, but one of them is that the dealers should have the right to become truly independent businessmen and purchase their locations. In the past year, we have made a study of the retail market in several countries which share the same international oil companies as we do in the United States. In almost every case, these same refiners have achieved domination in the oil industry to where they now control the retail market and its prices in that country by simply eliminating competition. For example, in Canada, a concentration of power in the hands of six refiners enables them now to set the retail prices in more than 90 percent of the service stations in Canada. The former independent dealers are now commissioned agents.

In Australia, a railroad strike and a huge increase in automobile use last July—when I happened to be there—saw these same companies simultaneously increase the price of their gasoline 25 cents per gallon overnight. It was almost unbelievable.

Most of these countries now have special commissions working on recommendations to restore competition to their gasoline markets. In most cases, it is too late. Canada's commission recently recommended that dealers who have been captive customers of their suppliers be allowed to buy product from any source, and that companies divest themselves of 50 percent of their retail outlets.

Our concern is that the fate of the retail market in these countries might very well be our fate. And I think we need some reassurance that it will not be our fate. I think we need some safeguards in future mergers that should refer specifically to what is going to happen to these small businesses which so often constitute the marketing network of major oil companies.

Thank you, Senator.

Senator HATCH. Thank you

Mr. Rothschild.

Mr. ROTHSCHILD. Thank you, Senator Hatch.

My name is Edwin Rothschild. I am the assistant director of the Citizen Labor Energy Coalition. We are a nationwide coalition of senior citizen, labor union, consumer, citizen organizations.

There are a lot of things that I want to discuss in the short time that I have, Senator. I want to start off first by putting something in the record that I had not intended to, but I think it bears on this issue.

On December 4, a letter I wrote was published in the New York Times, talking about splitting Gulf, basically, praising what Mr. Pickens was doing in an effort to create more competition in the industry; that he might spin off some of the properties, the refineries, so that the refiners could get into the business of competing for oil and maybe bargaining down the price, which is, of course, artificially high in the marketplace today.

Senator HATCH. Without objection, we will put that in the record at this point.

[Letter not available at press time.]

Mr. ROTHSCHILD. I received a letter dated December 22d from none other than Mr. Pickens. It was a very short letter, and I will read it:

I read with great interest your letter to the Editor in the December 4th, 1983 issue of the New York Times. I appreciate your taking the time not only to analyze

Dillard Spriggs' view on the implications of the Gulf Investor Group's actions, but also to express that view for the benefit of other readers. Boone Pickens.

Then, a P.S., in his own writing:

It was an excellent letter, right on the mark.

So I am somewhat shocked today that he can come here and say he is for these mergers, when I thought that what he really was about was to create more competition in the industry. I think that is the central problem that we are facing today with these mergers that come on the heels of many other mergers.

Let us start with the crude business. We have heard that there is plenty of competition in the crude business. I will dispute that. Part of my testimony contains charts showing the current reserves and the postmerger reserves if all of these three mergers take place. The top eight companies, if these mergers go through, will have 50 percent of the crude oil market, but that is understated by 14 percent, because as the FTC pointed out in its 1982 merger study, these oil companies control also the royalty share; they pay the royalty owners in cash. They have the control of the oil. So you have to add another 14 percent. That means that the ownership would go from 51 to 57 percent. But that is not where it ends. On top of that, the majors, for the most part, control the gathering lines into the fields, so they not only have control over their own oil, the royalties on the oil, but the other owners in the field. If there happens to be a small oil company that does not have any refining, it is the major who gets control of that oil through the ownership of the gathering lines. They post the price in the field.

What happened a few months ago, when an independent company, Ashland, and another refiner tried to lower prices in the field by $1.50, they were descended upon and had to raise their price after the majors clobbered them in the marketplace and said, "You can't do this. We are not going to allow you to do that."

There is very little competition at the domestic oil level, not only because of this, but on top of that—and all of these things are in this FTC report—because of the joint venture arrangements among the companies, where they coordinate production.

Interdependence, not independence, not aggressive competitiveness, which we expect in a free enterprise economy. That is not happening, and it is not happening at the crude level. Sure, there are independent drillers going out there, looking for oil. There is competition in the search for oil, in the acquisition of leases. But that is not what we are talking about once the oil is being produced.

What about the pipeline industry? Over 90 percent, according to the FTC again, of oil shipments in the country are controlled by the major companies through their ownership, both individually and jointly, of the pipelines. They control the network.

We have an FERC that is unwilling to regulate that on behalf of the consumers. The U.S. Court of Appeals for the District of Columbia circuit threw back the *Williams Brothers* case when they said these are not just and reasonable prices. So they are allowing the pipelines to keep prices high. In fact, the FTC points out in its Texaco-Getty acquisition that Colonial Pipeline, that ships almost

half the oil to the east coast, makes a 22-percent return on investment, which is extraordinarily high for a regulated utility.

Going on, the companies also are dominant—and you have to look at this. This is not a national market. Oil is unlike steel. We do not have a national market in oil. Oil is marketed on a regional basis, and if you are going to understand like the FTC, at least on an analytical side, they analyze it on a regional basis. Refiners on the gulf coast, on the east coast, and the west coast, the top four companies on gulf coast refiners, 58 percent; premerger, top eight—excuse me, that was just in Texas—the entire gulf coast, the top 8 before the merger were 59; after the mergers, 63 percent. And it goes on.

I will also put in the record heating oil sales by State, which were put out by the Department of Energy in 1979, and in almost every State, these shares are very, very high by the top eight companies. In Oklahoma, the top eight companies, 96 percent; in Alabama, 93 percent; Ohio, 78 percent; South Carolina, 86 percent, and so forth.

So the real problem, Mr. Chairman, as the court, the U.S. Court of Appeals, when it stopped the Mobil-Marathon merger, said, this industry is not competitive. It is filled with joint venture, anticompetitive, structural problems, and that is why that merger was stopped.

And finally, Mr. Chairman, even the former Assistant Attorney General, Mr. Baxter, who created part of the problem in the first place by basically saying: "Go ahead and merge; we are not going to enforce the antitrust laws"—well, it is nice to have antitrust laws, but if nobody is out there enforcing them, consumers are not being protected. That competitive market is not being allowed to thrive. That Assistant Attorney General said that Mobil, Texaco, and Socal and Exxon, the Aramco partners, along with Saudi Arabia, engaged in practices to reduce production in Saudi Arabia that may have cost consumers in the United States $1 billion.

Now, these are the kinds of companies and arrangements that we have to look at when we look at mergers, because the mergers are going to even further consolidate an industry that is heartily competitive in today's market.

One last point, Senator, and I know I am over the time. It was mentioned that this particular legislation, which we support—we think the period should be longer, but we still support the moratorium—is particular, because it is picking out a particular industry, and it is picking out a particular set of companies, and it is retroactive. Well, plenty of legislation that is passed by Congress has those problems to it, but it is still in the public's interest, and that is why legislation is passed. I can look at the U.S. Tax Code, and we can go through year-by-year, looking at which industries and which businesses benefit from the U.S. Tax Code through legislation that is passed. Similarly, the Natural Gas Policy Act, which was passed in the fall of 1978, was retroactive to April 1977. So, as far as those are concerned, I see no problems there. I think the public policy questions of whether this is good for the country, not just for stockholders, but good for the entire country, the marketplace, the consumers—those are the questions that ought to be addressed, and they ought to be addressed so that the Senate can have some time

to deliberate, and the House can deliberate on this in the 6-month moratorium.

Thank you.

Senator HATCH. Thank you, Mr. Rothschild.

[The following was received for the record:]

Statement of Edwin Rothschild

Assistant Director

Citizen/Labor Energy Coalition

before the

Committee on the Judiciary

United States Senate

March 15, 1984

Mr. Chairman and members of the Committee. My name is Edwin Rothschild. I am the Assistant Director of the Citizen/Labor Energy Coalition, a nationwide coalition of over 300 citizen, senior, labor, and church groups working on behalf of its 13 r'llion members for reasonably priced energy supplies.

We very much appreciate the opportunity to testify on the question of whether or not Congress should pass legislation restricting or prohibiting mergers among the nation's largest oil and energy companies.

We believe, based upon evidence available in numerous government studies, congressional hearings and court cases that mergers among the nation's top 20 oil companies should be prohibited and that proposed mergers between any of the top 20 companies with energy companies whose assets exceed $1 billion ought to be subject to a six month moratorium, so that a full-fledged congressional investigation can fully analyze the consequences of such mergers for the nation's economy, the oil and energy industries and energy consumers.

We also support the legislation proposed by Senators Johnston, Metzenbaum and Rudman which would declare a moratorium for six months on large mergers effective February 28, 1984. A particularly useful part of their legisation is the creation of a c nittee made up of four senators, four representatives and s..eone appointed by the President to study all major aspects of oil company mergers.

Congress must act swiftly on this issue. Without such action, it is almost certain that the pro-trust members of the Federal Trade Commission will allow these mergers to be consummated and the industry to be further consolidated.

The FTC already has issued its preliminary approval of the takeover of Getty Oil by Texaco, Inc. and is likely to provide similar approval to the proposed merger between Standard Oil of California and Gulf Oil and between Mobil Oil and Superior Oil. All of these mergers must be prohibited, because, in addition to misallocating capital and fueling further stock speculation, they will result in increased concentration, a lessening of competition and a greater ability to maintain prices above competitive market levels.

MERGERS MISALLOCATE CAPITAL

In our view mergers among the nation's largest oil companies are not in the public interest. While such mergers certainly

benefit the stockholders -- primarily large banks and financial institutions -- of the acquired firm; 1 the Wall Street arbitragers who make lots of money speculating on the increased value of the stock; the financial consultants, lawyers and accountants, whose technical expertise is handsomely compensated; 2 and of course, the acquiring company which obtains vast new assets, the rest of the country pays.

These mergers misallocate billions of dollars, because money is not being spent on productive investments. As Nobel Prize winning economist Wassily Leontief has observed mergers do not produce "new assets or new jobs -- nothing is added to the economy." Money raised to finance mergers or to defend against hostile mergers is money not available for other uses. As The New York Times reported regarding the mergers taking place in 1981,

> According to the Federal Reserve Board, $47 billion in lines of credit were extended for acquisitions by banks in the United States in the last half of 1981 alone. The Fed estimates that $20 billion to $21 billion of those takeover loans were actually drawn down, an amount that equalled the increase in total business loans in the United States between June and December 1981.

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1. According to The Wall Street Journal, March 7, 1984, at least 63 percent of Gulf shares are held by stock speculators and institutional investors. The group led by T. Boone Pickens, for example, holds 21.7 percent, arbitragers have 20 percent and the Mellon Bank has nearly 10 percent of the stock.

2. Reported transaction fees for the DuPont/Conoco merger were over $42 million and nearly $38 million for the U.S. Steel/Marathon merger.

> These huge loan commitments, made at a time of tight monetary policy, tend to drive up interest rates because, as several banking studieshave shown, banks with such commitments lose the flexibility to ration credit and thus must restrict borrowing by raising rates. 3

Indeed, money will have to be spent by Mobil, Socal and Texaco to repay the loans incurred for their $30 billion takeovers. This may sharply reduce the money spent on drilling for new reserves, particularly in view of the fact that their newly acquired reserves are so plentiful. Between 1978 and 1982 Standard of California, for example, discovered the equivalent of 602 million barrels of oil and gas in the United States. By acquiring Gulf they not only obtained 1.4 billion barrels of oil and natural gas in the U.S., but also over 2 billion tons of coal and large quantities of other mineral resources and nearly 13 million acres of potential oil and gas producing leases in the U.S. alone. Oil analyst Paul Mlotok of Salomon Brothers also believes that the merged entity will spend less on exploration than the separate companies would have spent. As a result, he believes "Eventually this trough in exploration would lead to a trough in production, which would work to OPEC's benefit." 4

en the former chairman of Standard Oil of Indiana agrees that these large mergers may mean a reduction in the amount of money spent on exploration by newly combined entity. "I think some industry revenues will be diverted from that purpose to pay off the debt. But when the debt is paid down--it may take five or ten years--then you'll have a stronger company, which may in the long run do more drilling." 5 That is not the kind of positive response Swearingen has been known for. In fact, it reinforces the concern expressed by many Members of Congress that these mergers are contrary to what the oil industry promised in return for oil and natural gas decontrol.

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3. The New York Times, May 3, 1982. See also, "Letters," The New York Times, January 10, 1982:

> Estimates published in The Times in August would indicate that the amount of bank credit used for acquisitions in 1981 will equal or exceed $70 billion. So, if bank credit for mergers had be cut off in 1981,the effect on the money markets would have been the same as balancing the Federal budget for the year.

4. Oil & Gas Journal, February 27, 1984.

5. The New York Times, March 11, 1984.

WHERE'S THE PAYOFF FROM OIL DECONTROL?

When Congress was considering President Carter's decision to phase out price controls on domestically produced crude oil and whether or not to impose a windfall profits tax, oil industry executives argued vehemently in opposition to the tax and in favor of decontrol. They said that the money generated from decontrol was desperately needed to support increased exploration. In May 1979 the former chairman of Gulf Oil, Jerry McAfee, told the House Ways and Means Committee that "the industry will spend any increased earnings from decontrol in the continued search for energy in the United States." Three years later Charles DiBona, the head of the American Petroleum Institute, in his criticism of the windfall profits tax went so far as to say that the revenues generated by decontrol and "retained by producing companies will fall far short of their future needs, even without additional taxes." 6

Oil decontrol, which was estimated to cost consumers about $50 billion for the 1979-1981 period, 7 provided the major oil companies with far more income than they needed or were willing to invest in increased expenditures for domestic exploration and production. This is clearly demonstrated by comparing what happened in the three years prior to decontrol with the three years following decontrol.

In the three years following decontrol (1979-1981), the nation's 16 largest oil companies increased their exploration and production earnings by 147 percent compared to the three years prior to decontrol. Yet, over the same period these companies raised their spending on exploration and production by only 115 percent while increasing their expenditures on mergers and acquisitions by 600 percent. 8

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6. Testimony before the Committee on Interstate and Foreign Commerce, House of Representatives, May 16, 1982.

7. "The Energy Inflation Crisis: Sources, Consequences, and Policy Options," Report by the Subcommittee on Oversight and Investigations of the Committee on Interstate and Foreign Commerce, House of Representatives, December 1980.

8. "Spending the Windfall: An Analysis of Post-Decontrol Oil Company Acquisitions and Investments," A Research Report by the Citizen/Labor Energy Coalition, June 1982.

While some may argue that an increase of 115 percent is large, this rate of increase fell far short of the rate of increase for profits. "The oil exploration business (is) more profitable than any other segment of American industry," according to Merrill Lynch in 1982. Thus, it is particularly surprising that the companies did not invest at a rate in excess of their earnings. The reason is that decontrol (even with a Windfall Profits Tax) generated far more capital than the companies have been able or willing to invest. The companies spent as much of their increased cash flow

9 to acquire competitors, other industrial firms and non-petroleum activities, as they spent on U.S. exploration and production.

It is interesting to note that today, when public discussion is centered on the social and economic utility of large oil company mergers, oil company executives no longer discuss the need for more revenue to expand drilling efforts and to make the U.S. less dependent on foreign oil. Instead, we are told that there is plenty of capital available for drilling, but that what is unavailable are, according to T. Boone Pickens, "drillable

prospects." 10

Bankrolled by the billions of dollars from oil decontrol and the partial decontrol of natural gas, the merger mania sweeping through the oil/energy industry is also being driven by several other factors, including lax antitrust enforcement, federal tax incentives, riskless reserve additions, stock speculation, and the further reduction of competition.

Lax Antitrust Enforcement

The Federal Trade Commission has signalled its intention to allow mergers between large competitors in the petroleum industry, despite evidence demonstrating such mergers will be anti-competitive and despite growing congressional, industry and consumer opposition. Moreover, the Secretary of Energy has

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9. Cash flow is the funds a firm has available to it to make investments and to pay dividends to shareholders. Cash flow consists of profits, other funds generated by operations (e.g. deferred taxes and depreciation), and capital raised by borrowing money or issuing stock. Cash flow, not profits, is the measure financial analysts and economists use to evaluate the investments and performance of companies.

In comparing the two three-year periods, the total cash flow available to the 16 top oil companies increased by $77.1 billion (from $84.1 billion in the 1976-78 period to $161.2 billion in the 1979-81 period). Of this $77.1 billion of marginal cash flow, $26.7 (35%) was used for acquisitions and non-petroleum investment.

10. The MacNeil/Lehrer News Hour, March 6, 1984

stated publicly that the top 20 companies are "very big, big c panies, very capable of competing," and that "the mergers don't seem to me to be cutting across that significantly." 11

The revised merger guidelines issued when William Baxter was in charge of the Justice Department's Antitrust Division was the Administration's signal to companies, who had previously resisted the temptation for fear of vigorous antitrust enforcement, that their merger proposals would probably meet with Administration approval. Baxter rewrote the merger guidelines because he believed that the government should allow mergers "which promote efficiencies." 12

Baxter was even more specific regarding oil industry mergers in an August 1981 interview. He said that there was a surge of merger activity among oil companies because the companies "are flush with cash...and they're looking for effective ways to deploy large holdings." He stated further that the Reagan Administration's antitrust policy "is different from that of previous administrations, and people are contemplating mergers t t they would have been somewhat more bearish about before." In response to a question asking if there were some contemplated mergers that companies would not have considered in the past, Baxter said, "Mobil Corporation's tender offer for Conoco might fall into that category. If Texaco makes an offer for Conoco, I would put that in the same class." Baxter also told potential merger candidates that if there were areas of "horizontal overlap," the merger could be "saved by pruning one or the other of the partners, carving out a subsidiary prior to the merger." 13

The Federal Trade Commission adopted Baxter's new theoretical and permissive posture to large mergers, when it ruled favorably on Mobil's attempt to acquire Marathon Oil and approved the takeover of Getty Oil by Texaco. While the FTC required Texaco to divest certain refining, marketing and transportation assets and to make a commitment to continue to supply certain Getty customers upon completion of the merger, this remedy does more harm than good. The Commission permits Texaco to retain all of

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11. The New York Times, March 11, 1984

12. Confirmation Hearing on William F. Baxter, Nominee, to be Assistant Attorney General -- Antitrust Division, Committee on the Judiciary, United States Senate, 97th Cong., 1st Sess., March 19, 1981, p. 59.

13. U.S. News & World Report, August 3, 1981

Getty's crude oil and natural gas reserves, its crude oil gathering systems, its large East Coast refinery and other assets most desired by Texaco. It requires Texaco to divest a Getty refinery in El Dorado, Kansas and Getty's interest in a pipeline which delivers refined products from the Kansas refinery to markets in Colorado. Under the FTC arrangement, however, Texaco has no obligation to supply this refinery with oil. As a result, there is a good chance this refinery will be shut down, leading to reduced competition in the markets it serves. In California, the FTC's proposal requires Texaco to sell crude oil at the "posted price" for a period of five years to independent refiners. FTC Commissioner Michael Pertschuk in his dissent from the Commission's decision explained how Texaco will still be able to manipulate supplies and prices in the California market. 14 It was precisely this kind of outcome that enforcement of the antitrust laws was supposed to prevent.

Federal Tax Incentives

The tax consequences of mergers are significant. Depending on the type of acquisition, how it is being financed and how the shareholders of the acquired firm are compensated, the U.S. tax code may provide tax-related benefits to the combined firm. In 1982 the Federal Trade Commission observed that "The ability to step up the basis of an acquired firm can provide a substantial incentive for merger by allowing the combined firm to redepreciate assets and reduce tax liabilities." 15 And Robert J. Samuelson recently pointed out that "When profitable companies borrow, they deduct interest costs from their taxes, which -- because the top corporate tax rate is 46 percent -- means the true interest rate is about half the market level." 16

As part of any legislative proposal dealing with these mergers, Congress ought to couct a thorough examination of the tax implications and consequences of these and other mergers. To what degree are other American taxpayers helping to finance these multi-billion dollar deal?

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14. In the Matter of Texaco Inc. and Getty Oil Company, "Agreement Containing Consent Order," File No. 841-007, Federal Trade Commission, February 13, 1984

15. Mergers in the Petroleum Industry, A Report of the Federal Trade Commission September 1982, p. 80

16. The Washington Post, March 14, 1984.

Acquiring Riskless Reserves

The major oil companies recognize that while the costs of finding oil through drilling may be comparable to the costs of buying reserves through acquisition, 17 the risks are quite different. There is very little uncertainty in buying known quantities of already discovered reserves. There is a great deal of uncertainty in exploring for large fields, as the recent experience with the Mukluk well in Alaska demonstrates.

Large oil companies are interested in obtaining large reserves of oil and gas. Finding such reserves through acquisition does not require years of exploratory work. It also guarantees a one hundred per cent success rate. The table below indicates that between 1978 and 1982 Texaco found the equivalent of 553 million barrels of oil in the U.S. and spent $6.6 billion. By acquiring Getty it obtains, in addition to all of Getty's other assets, 1.6 billion barrels, three times the amount it found over a five-year period. Over the same period Socal found 682 million barrels and spent $7.7 billion. By acquiring Gulf, Socal obtains more than twice the reserves -- over 1.4 billion barrels -- than it found. Mobil's purchase of Superior nets it slightly more reserves -- 447 million barrels -- than it found over the 1978-82 period -- 428 million barrels.

Undervalued Stocks

Because stock speculators believe in making short-term profits, while oil company managements believe in long-term profit maximization, and because there often can be a substantial discrepancy between the value of an oil company's underlying assets and the stock price reflecting those assets, a number of oil companies have become vulnerable to takeovers. The exploitation of this difference allows stock speculation and the kind of management panic so effectively promoted by T. Boone Pickens.

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17. One recent analysis even concluded that "it is less costly to acquire a BOE (barrel of oil equivalent) by drilling than by acquisition." "The Cost of Reserves By Discovery vs. Acquisition," James C. Dyer, Oil & Gas Journal, December 19, 1983.

According to Pickens, a number of major companies are wasting their huge cash flows from previous discoveries to finance exploration for more costly and difficult to find reserves, on non-oil investments like Exxon's acquisition of Reliance Electric and on subsidizing unprofitable refining and marketing (rations. This is why, according to Pickens and others, a number of companies are price around 40% of their asset value.

18

Executives of the major companies, says Gulf Oil's chairman James Lee, "have to be concerned about the long-term viability"

of their corporations. 19

No matter whose strategy is correct, the end result of this wasteful clash corporate and financial muscle is the further consolidation of the industry in fewer hands. A restriction or prohibition on merger activity would freeze on any more efforts by Pickens and others to make hundreds of millions of dollars in the stock market manipulation, which some observers have suggested is Pickens' real intent.

Reduced Competition

The elimination of a large competitor from the ranks of the oil industry provides the acquiring company with more control over the price it can charge for its products. With increased concentration of ownership and control over production, transportation, refining and marketing, the largest companies in the industry will be in an even stronger position to limit competition from independent refiners and marketers.

Consumers lose when competition is reduced, because prices will be established and maintained at levels above those obtaining in a competitive market. Increased control over geographic and product markets by fewer firms means that consumers of gasoline, heating oil and other products will be forced to pay excessively high prices.

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18. Fortune, December 26, 1983

19. Business Week, November 14, 1983.

THE ANTI-COMPETITIVE STRUCTURE OF THE DOMESTIC OIL INDUSTRY

'nlike the Federal Trade Commission, the U.S. Court of Appeals for the Sixth Circuit in 1981 blocked Mobil's proposed merger with Marathon Oil on antitrust grounds. In its ruling the Court cited evidence demonstrating "that the oil industry is characterized by a complex set of close working relationships; joint ventures for crude oil exploration and production; joint operation of pipelines and transportation; exchange agreements under which the companies swap among themselves crude oil and refined products..." 20 The "complex set of close working relationships" is nothing new. It has characterized the structure and operation of the major oil companies since the breakup of the Standard Oil Trust in 1911.

For example, evidence compiled before the Temporary National Economic Commission, set up by Congress in 1938 to conduct a study of the concentration of economic power in American industry and the effect of that concentration upon the decline in competition, found concentration in the oil industry high at every level. Congressional investigations by the Antitrust and Monopoly Subcommittee under Senator Estes Kefauver and Senator P lip Hart provided continuing evidence that the oil industry, both domestically and internationally, was not workably competitive.

In 1973 the Federal Trade Commission filed an antitrust complaint against the eight largest oil companies. Although the Reagan Administration put an end to the litigation, the Commission staff through the discovery process obtained a vast number of industry documents showing that the companies engaged in "a common course of action, the ultimate purpose of which was to maintain and reinforce the noncompetitive market structure at every level of the petroleum industry." 21

The FTC staff concluded that among the effects of the companies' actions were:

1) the establishment and maintenance of artificially high price levels for both domestic and foreign crude oil;

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20. 669 Fed. 2nd 378, December 23, 1981

21. In Re:Exxon, et. al., Docket No. 8934, "Complaint Counsel's First Statement of Issues, Factual Contentions and Proof, October 31, 1980.

2) foreclosure and suppression of actual and potential competition in the refining and marketing segments of the industry (accomplished, in part, by the respondents uniform exploitation of their ownership of pipelines to control supply and distribution of crude oil and refined products); and ultimately

3) the payment of substantially higher prices by American consumers for refined petroleum products than they would have paid in a competitively structured market.

Even former Assistant Attorney General William Baxter concluded that,

> ...between 1974 and 1979 the Saudis, either directly or in conjunction with the Aramco partners [Exxon, Socal, Texaco and Mobil], were able, by adjusting their output, to prevent significant fluctuations in the world price of oil despite a significant recession, high inflation and a substantial increase in non-OPEC production capacity.

22 Baxter also concluded that the Aramco partners in 1975 may have restricted Saudi crude production "for anticompetitive reasons." The ability of the Aramco partners to withhold Saudi output, said Baxter, "could have cost U.S. consumers in excess of $1 billion annually."

These findings are not unique. The results of the Canadian government's investigation, "The State of Competition in the Canadian Petroleum Industry," found that the multinational petroleum companies "that dominate the Canadian industry have used various restrictive practices to develop, protect, and exploit their monopolistic situation in Canada."23 Based on this investigation, the staff of Canada's Restrictive Trade Practices Commission filed an 830-page report which calculated consumer overcharges of $3.2 billion from 1958 to 1973, adjusted for inflation. According to The New York Times, "The report is the broadest investigation of the oil business ever undertaken in the world." [The New York Times, February 23, 1984]

The basic problem with the domestic oil market is that sufficient competition is lacking at most industry levels and in many geographic areas of the country. Large mergers will even further reduce competition.

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22. "Memorandum for the Attorney General, Re: Termination of the Antitrust Division's International Oil Investigation," December 7, 1983

23. Volume I, Findings, Issues and Remedies, February 27, 1981, p. 35.

THE CRUDE OIL MARKET

Even though the market for crude oil is international and even though major international oil companies no longer own oil resources in most of the OPEC countries, they are still among the largest producers and buyers of oil worldwide. The major international oil companies still produce their own crude oil in the United States, Canada, the North Sea and several other countries. In some OPEC countries, the major oil companies still produce equity oil [as in Indonesia and Nigeria]. In most other OPEC countries, the majors have contracts to purchase the output, or, as in the case of Saudi Arabia, are virtually the sole purchasers. This combined producing and purchasing power still provides the majors with the ability to allocate supplies and with OPEC manage production.

At the beginning of 1983 in the United States the top 8 oil companies owned about 44 percent of the nation's oil reserves and 39 percent of oil production (See Tables I and III). If the mergers between Texaco/Getty, Socal/Gulf and Mobil/Superior are permitted, the largest eight companies will own 50 percent of the reserves and 45 percent of production. But these figures vastly understate the real control these companies exercise over reserves and production.

The Federal Trade Commission has reported:

> In general, petroleum firms do not own the land on which they produce oil. Instead, the producer typically enters into an oil and gas lease, which allows the oil producer to drill wells on the land and recover the crude oil [or natural gas] found. As payment for this concession, the producer will customarily assign the landowner a royalty share (usually 1/8) of the crude oil produced. Because the landowner is not normally a participant in the petroleum industry, this share will most often be taken in cash. Thus, in the most common arrangement of this type, for every seven barrels reported as a part of the firm's owned production, an additional barrel of royalty oil will be under the control of the firm for purposes of sale or other disposition. To the extent that royalty oil is excluded from reported production, market share figures for leading firms could be understated by as much as 14 percent. 24

Thus, adjusting the top 8 companies share by 14 percent results in pre-merger concentration of 51 percent and post-merger concentration of 57 percent. But, the FTC found that control is also exercised through the ownership of gathering lines which " ..y enhance to some degree the market power held by the larger

firms." 25 A Congressional committee staff study found that in 1974, in Texas, the 20 largest oil companies together gained physical control through gathering of an additional amount of crude oil equivalent to 13.1 percent of their Texas production. 26

It is interesting to note that the above-cited FTC study on petroleum industry mergers concluded that "These arrangements, consisting of crude oil joint bids for federal and state oil and gas lands, joint drilling ventures, crude exchanges, ownership of crude gathering and transportation systems, should therefore be examined in assessing the impact of particular mergers on competition." So far, in reviewing the Mobil/Marathon merger in 1981 or the Texaco/Getty merger this year, the Commission has failed to examine these arrangements and the impact the proposed mergers would have at the level of crude oil production.

Tables II and IV show the changes in concentration levels for n..ural gas reserves and natural gas 'production, respectively. This data, however, is not relevant to an analysis of competition in the sale of natural gas, because most of the nation's gas reserves are committed to long-term contracts and are thus not part of "the market." As of December 31, 1982 21.5 Tcf of natural gas reserves were uncommitted and 152.2 Tcf were committed. In analyzing the producer natural gas market, the Committee ought to obtain market share data of uncommitted gas reserves on both a national and producing area basis.

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24. "Mergers in the Petroleum I.. ustry," Report of the Federal Trade Commission, September 1982, p. 159.

25. Ibid., p. 160.

26. Subcommittee on Monopolies and Commercial Law, Committee on the Judiciary, House of Representatives, 96th Cong., 1st Sess.,"Interdependence in Domestic Crude Oil Joint Ventures, Farm Outs, Exchanges, and Gathering Lines," 1979.

OIL PIPELINES

In addition to their control over most of the crude oil gathering lines, the major companies also control, individually and jointly over 91 percent of crude oil and petroleum products shipped through the nation's large-diameter pipelines. The major companies accounted for ownership of over 74 percent of total pipeline mileage. Because of this control, concentration of oil shipments in regional marketing areas is very high. Table VIII identifies four of the nation's largest and most important pipelines and their owners. In its 1982 Merger Study, the FTC concluded,

> Because of the potential economies of scale of certain pipelines, the possibility of market power exists. The degree of such market power will often depend on the size of the pipeline, which may confer unique competitive advantages upon it in comparison with other, smaller pipelines or alternative modes of transportation in a given service area (p. 246). Even though pipelines are supposed to be regulated, the Federal Energy Regulatory Commission has utterly failed to do its job. Just a few days ago a unanimous Court of Appeals for the D.C. Circuit in remanding the FERC's Williams Pipe Line case back to the Commission ruled that the FERC failed "to ensure that oil pipeline rates are "just and reasonable." [Slip Op. No. 82-2412.

In its analysis of the Texaco/Getty merger, the FTC staff found that the Colonial pipeline estimated it had a 20.22 percent return on equity for 1983, a rate of return far in excess of what a Commission concerned about "just and reasonable" rates would allow.

REFINING AND MARKETING

Concentration in the refining and marketing sectors of the oil industry are also extraordinarily high. As Tables V - VII show, the largest 8 refiners prior to the mergers already own 59%, 84% and 73% of the Gulf Coast, East Coast and West Coast markets, respectively. In combination with their ownership over the most efficient transportation modes, these companies also control the wholesale and retail sales of products such as gasoline and heating oil. Table IX, taken from a July 1979 DOE study entitled "Middle Distillate Market Profile Report" supports the view that in the key markets, eight companies produce and sell between 60% and 100% of middle distillate fuel. Similar information on regional control over wholesale and retail gasoline sales

is apparently in the hands of the Energy Information Administration of the Department of Energy.

CONCLUSION

Based on this evidence of high concentration at every level of the oil industry which, when combined with the vast network of joint venture relationships and vertical integration, one can only conclude that competition is minimal in the petroleum industry and that new mergers among the largest firms can only make a bad situation worse.

TABLE I
1982 U.S.LIQUIDS RESERVES
Thousands of Barrels

PRE-MERGERS			POST-MERGERS		
COMPANY	RESERVES	PERCENTAGE	COMPANY	RESERVES	PERCENTAGE
SOHIO	2855600	0.081	SOHIO	2855600	0.081
EXXON	2836000	0.081	EXXON	2836000	0.081
ARCO	2561000	0.073	ARCO	2561000	0.073
SHELL	2200000	0.063	TEXACO/GETTY	2246000	0.064
STD.INDIANA	1660000	0.047	SHELL	2200000	0.063
GETTY	1241000	0.035	SOCAL/GULF	2018000	0.058
SOCAL	1202000	0.034	STD.INDIANA	1660000	0.047
TEXACO	1045000	0.030	MOBIL/SUPERI	1044690	0.030
MOBIL	906000	0.026	SUN	691000	0.020
GULF	816000	0.023	MARATHON	606289	0.017
SUN	691000	0.020	UNION	523000	0.015
MARATHON*	606289	0.017	PHILLIPS	492000	0.014
UNION	523000	0.015	CONOCO	350000	0.010
PHILLIPS	492000	0.014	OCCIDENTAL	275000	0.008
CONOCO**	350000	0.010	AMERADA HESS	260000	0.007
OCCIDENTAL***	275000	0.008	TENNECO	251181	0.007
AMERADA HESS	260000	0.007	CHAMPLIN	152900	0.004
TENNECO	251181	0.007	PENNZOIL	140000	0.004
CHAMPLIN	152900	0.004	SANTA FE	138300	0.004
PENNZOIL	140000	0.004	MITCHELL	125899	0.004
TOP 4	10452600	0.298		10498600	0.299
TOP 8	15600600	0.444		17421290	0.497
TOP 16	20259889	0.577		20869760	0.595
TOP 20	21063970	0.599		21426859	0.611
TOTAL US	35079000				
	11915964	0.340		11960404	0.341
	17784684	0.507		19860271	0.566
	23096273	0.658		23791526	0.678
	24012926	0.685		24426619	0.696

* Acquired by U.S. Steel.
** Acquired by DuPont.
*** Acquired Cities Service.

Source: Oil & Gas Journal, October 17, 1983.

TABLE II
1982 U.S. NATURAL GAS RESERVES
Billions of Cubic Feet

PRE-MERGERS			POST-MERGER		
COMPANY	RESERVES	PERCENTAGE	COMPANY	RESERVES	PERCENTAGE
EXXON	16461	0.078	EXXON	16461	0.078
ARCO	14438	0.069	ARCO	14438	0.069
STD.INDIANA	9009	0.043	STD.INDIANA	9009	0.043
SHELL	7290	0.035	SOCAL/GULF	8947	0.043
SOHIO	6391	0.030	TEXACO/GETTY	8643	0.041
MOBIL	6334	0.030	MOBIL/SUPERI	8189	0.039
TEXACO	6247	0.030	SHELL	7290	0.035
UNION	5170	0.025	SOHIO	6391	0.030
SOCAL	5046	0.024	UNION	5170	0.025
GULF	3901	0.019	PHILLIPS	3432	0.016
PHILLIPS	3432	0.016	TENNECO	3207	0.015
TENNECO	3207	0.015	SUN	3148	0.013
SUN	3148	0.015	OCCIDENTAL	2747	0.011
OCCIDENTAL	2747	0.013	CONOCO	2303	0.011
GETTY	2396	0.011	CHAMPLIN	2021	0.010
CONOCO	2303	0.011	MARATHON	1891	0.009
CHAMPLIN	2021	0.010	PANHANDLE	1333	0.006
MARATHON	1891	0.009	TEXAS O&G	1253	0.006
SUPERIOR	1850	0.009	COASTAL	1059	0.005
PANHANDLE	1333	0.006	NORTHWEST	1050	0.005
TOP 4	47198	0.224		48855	0.232
TOP 8	71340	0.339		79368	0.377
TOP 16	97520	0.463		103287	0.491
TOP 20	104615	0.497		107982	0.513
TOTAL US	210512			210512	
	53806	0.255		55695	0.265
	81328	0.386		90480	0.430
	111173	0.528		117747	0.559
	119261	0.567		123099	0.585

Source: Oil & Gas Journal, October 17, 1983.

TABLE III
1982 U.S. LIQUIDS PRODUCTION
Thousands of Barrels

PRE-MERGER			POST-MERGER		
COMPANY	PRODUCTION	PERCENTAGE	COMPANY	PRODUCTIO	PERCENTAGE
EXXON	270000	0.074	EXXON	270000	0.074
SOHIO	253200	0.069	SOHIO	253600	0.069
ARCO	222000	0.060	TEXACO/GETTY	229000	0.062
ELL	190000	0.052	SOCAL/GULF	225000	0.061
STD. INDIANA	151000	0.041	ARCO	222000	0.060
TEXACO	127000	0.035	SHELL	199000	0.052
SOCAL	121000	0.033	STD. INDIANA	151000	0.041
GULF	104000	0.028	MOBIL/SUPERI	123787	0.034
MOBIL	103000	0.028	SUN	78000	0.021
GETTY	102000	0.028	MARATHON	58431	0.016
SUN	78000	0.021	UNION	55000	0.015
MARATHON	58431	0.016	PHILLIPS	50000	0.014
UNION	55000	0.015	CONOCO	50000	0.014
PHILLIPS	50000	0.014	TENNECO	34897	0.010
CONOCO	50000	0.014	AMERADA HESS	28000	0.008
TENNECO	34897	0.010	CHAMPLIN	21681	0.006
AMERADA HESS	28000	0.008	SANTA FE	16300	0.004
CHAMPLIN	21681	0.006	MITCHELL	16252	0.004
SUPERIOR	20787	0.006	LA. LAND	15100	0.004
SANTA FE	16300	0.004	AMINOIL*	14468	0.004
TOP 4	935200	0.255		977000	0.266
TOP 8	1438200	0.392		1663787	0.453
TOP 16	1969528	0.537		2039796	0.556
TOP 20	2056296	0.560		2101916	0.572
U.S. TOTAL	3671000			3671000	
	1066128	0.290		1113780	0.303
	1639548	0.447		1896717	0.517
	2245262	0.612		2325367	0.633
	2344177	0.639		2396184	0.653

Source: Oil & Gas Journal, October 17, 1983.

1982 U.S. NATURAL GAS PRODUCTION
Millions of Cubic Feet

PRE-MERGER			POST-MERGER		
COMPANY	PRODUCTION	PERCENTAGE	COMPANY	PRODUCTION	PERCENTAGE
EXXON	1035000	0.059	TEXACO/GETTY	1097000	0.063
TEXACO	778000	0.044	EXXON	1035000	0.059
STD. INDIANA	699000	0.040	SOCAL/GULF	946000	0.054
SHELL	607000	0.035	MOBIL/SUPERIO	874000	0.050
MOBIL	606000	0.035	STD. INDIANA	699000	0.040
GULF	525000	0.030	SHELL	607000	0.035
ARCO	470000	0.027	ARCO	470000	0.027
SOCAL	423000	0.024	UNION	403000	0.023
UNION	403000	0.023	TENNECO	390268	0.022
TENNECO	390268	0.022	SUN	321000	0.018
SUN	321000	0.018	PHILLIPS	274000	0.016
GETTY	319000	0.018	CONOCO	262000	0.015
PHILLIPS	274000	0.016	PENNZOIL	168000	0.010
SUPERIOR	268000	0.015	TEXAS O&G	133823	0.008
CONOCO	262000	0.015	MARATHON	132977	0.008
PENNZOIL	168000	0.010	CONSOL NG	122000	0.007
TEXAS O&G	133823	0.008	AMERADA HESS	109500	0.006
MARATHON	132977	0.008	CHAMPLIN	100770	0.006
CONSOL. NG	122000	0.007	COASTAL	100971	0.006
AMERADA HESS	109500	0.006	PANHANDLE EAS	97552	0.006
TOP 4	3119000	0.178		3954009	0.226
TOP 8	5143660	0.294		6133000	0.350
TOP 16	7548268	0.431		7937068	0.453
TOP 20	8046568	0.460		8353861	0.477
TOTAL U.S.	17506000			17506000	
	3555660	0.203		4507560	0.257
	5863020	0.335		6991620	0.399
	8605026	0.492		9048258	0.517
	9173088	0.524		9523402	0.544

Source: Oil & Gas Journal, October 17, 1983.

TABLE V

GULF COAST REFINERIES

Texas	Cap. (b/cd	Percent	Louisiana	Cap. (b/cd	Percentage
Exxon	427000	0.125	Exxon	419000	0.205
Amoco	415000	0.121	Cities Ser	297000	0.145
Shell	285000	0.083	Marathon	255000	0.125
Mobil	277000	0.081	Shell	218000	0.107
Gulf	268400	0.079	Gulf	199100	0.098
Texaco	242000	0.071	Conoco	156500	0.077
Arco	232000	0.068	Texaco	140000	0.069
Phillip	175000	0.051	Tenneco	114000	0.056
Union	120000	0.035			
Maratho	49000	0.014			
Conoco	33274	0.010			
Sub-tot	2523674	0.738		1798600	0.881
Top 4	1404000	0.411		1189000	0.582
Top 8	2321400	0.679		1798600	0.881
TOTAL	3417724	1.000		2041900	1.000

Mississ	Capacity	Percentage	Alabama	Capacity	Percentage
Socal	280000	1.000		131600	1.000

GULF COAST - PRE-MERGER			GULF COAST - POST-MERGER		
Exxon	846000	0.144	Exxon	846000	0.144
Shell	503000	0.086	Socal/Gulf	747500	0.127
Gulf	467500	0.080	Shell	503000	0.086
Amoco	415000	0.071	Amoco	415000	0.071
Texaco	382000	0.065	Texaco	382000	0.065
Marathon	304000	0.052	Marathon	304000	0.052
Socal	280000	0.048	Mobil	277000	0.047
Mobil	277000	0.047	Arco	232000	0.040
Arco	232000	0.040			
Conoco	189774	0.032			
Phillips	175000	0.030			
Union	120000	0.020			
Sub-Total	4191274	0.714			
Total	5871224	1.000			
Top 4	2231500	0.380	Top 4	2511500	0.428
Top 8	3474500	0.592	Top 8	3706500	0.631

Source: Department of Energy.

TABLE VI
EAST COAST REFINERIES

STATE	COMPANY	CAP. b/cd	PERCENT
Delaware			
	Getty	140000	0.111
Georgia			
	Amoco	24000	0.019
M. /land			
	Socal	14200	0.011
New Jersey			
	Exxon	100000	0.079
	Mobil	99700	0.079
	Texaco	90000	0.071
	Socal	80000	0.064
Pennsylvania			
	Gulf	174100	0.138
	BP Oil	168000	0.133
	Sun	155000	0.123
	Arco	125000	0.099
Sub-Total		1170000	0.929
TOTAL		1258950	1.000

EAST COAST REFINING AREA

PRE-MERGER			POST-MERGER		
Gulf	174100	0.133	Socal/Gulf	268300	0.213
BP	168000	0.133	Texaco/Getty	230000	0.183
Sun	155000	0.123	BP	168000	0.133
Getty	140000	0.111	Sun	155000	0.123
Arco	125000	0.099	Arco	125000	0.099
Exxon	100000	0.079	Exxon	100000	0.079
Mobil	99700	0.079	Mobil	99700	0.079
Socal	94200	0.075	Amoco	24000	0.019
Texaco	90000	0.071			
Amoco	24000	0.019			
Top 4	637100	0.506		821300	0.652
Top 8	1056000	0.839		1170000	0.929

Source: Department of Energy.

TABLE VII
WEST COAST REFINERIES

STATE	COMPANY	CAP. b/c	PERCENT
California	Socal	710000	0.306
	Union	197500	0.085
	Shell	184400	0.079
	Arco	178000	0.077
	Mobil	123500	0.053
	Exxon	106000	0.046
	Texaco	60000	0.026
	Gulf	51500	0.022
	Getty	38000	0.016
	Sub-Total	1648900	0.711
	TOTAL	2319990	1.000
Oregon	Socal	15000	1.000
Washington	Arco	126000	0.312
	Shell	91000	0.225
	Texaco	78000	0.193
	Mobil	71500	0.177
	Socal	5500	0.014
	Sub-Total	372000	0.920
	TOTAL	404470	1.000

PRE-MERGER			POST-MERGER		
Socal	730500	0.268	Socal/Gulf	782000	0.287
Arco	304000	0.112	Arco	304000	0.112
Shell	275400	0.101	Shell	275400	0.101
Union	197500	0.072	Union	197500	0.072
Mobil	195000	0.072	Mobil	195000	0.072
Texaco	138000	0.051	Texaco/Getty	176000	0.065
Exxon	106000	0.039	Exxon	106000	0.039
Gulf	51500	0.019			
Getty	38000	0.014			
Sub-Total	2035900	0.747			
TOTAL	2724460	1.000	Top 4	.572	
Top 4	1507400	0.553	Top 7	.733	
Top 8	1997900	0.733			

Source: Department of Energy.

TABLE VIII
MAJOR CRUDE OIL AND PETROLEUM PRODUCT PIPELINES

PRODUCT PIPELINES

Gulf Coast to East Coast (PADD III to PADD I)

Colonial (2303 MBD Cap.)		Plantation (825 MBD Cap.)	
Gulf	16.80	Exxon	48.80
Texaco	14.30	Socal	27.10
Amoco	14.30	Shell	24.00
Cities	14.00		
Mobil	11.50		
BP Oil	9.00		
Conoco	7.50		
Phillips	7.10		
Union	4.00		
Arco	1.60		

CRUDE PIPELINES

Trans-Alaska (1500 MBD Cap.)		From Gulf Coast to Midwest Capline (1200 MBD Cap.)	
BP/Sohio	49.18	Ashland	21.93
Arco	21.00	Marathon	15.69
Exxon	20.00	Texaco	15.09
Mobil	5.00	Shell	12.07
Phillips	1.66	Union	9.76
Union	1.66	Clark	9.76
Amerada Hess	1.50	Amoco	8.05
		BP/Sohio	5.10
		Sun	2.55

Source: "United States Petroleum Pipelines,
An Empirical Analysis of Pipeline Sizing,"
Department of Energy, December 1980.

EAST COAST REFINERY WHOLESALE GASOLINE PRICES
CENTS PER GALLON

ST	MONTH	MAJ. REF PRICE	MAJ. REF. VOLUME	OTH.REF PRICE	OTH. REF. VOLUME	DIFF. PRICE	MAJ VOL PERCENT
NJ	11/83	88.8	290062	84.6	13028	-4.2	0.957
	10/83	90.1	279504	87.3	11941	-2.8	0.959
	9/83	90.6	289814	84.2	15247	-6.4	0.950
	8/83	91.6	304786	88.9	11059	-2.7	0.965
	7/83	91.3	329217	88.8	25750	-2.5	0.927
	6/83	90.4	368817	86.8	16522	-3.6	0.957
	5/83	89.4	321027		18228		0.946
	4/83	87.9	321770	82.7	42779	-5.2	0.883
	3/83	84.7	308108	79.9	36804	-4.8	0.893
	2/83	87.9	240797				
	1/83	91.4					
GA	11/83	86.0	144784	83.4	41725	-2.6	0.776
		88.4	140639	85.4	41758	-0.3	0.771
		91.0	138447	88.2	39689	-2.8	0.777
		91.7	154089	89.1	38708	-2.6	0.799
		92.4	150848	89.8	35646	-2.6	0.809
		92.0	158359	90.1	33177	-1.9	0.827
		92.0	154439	89.9	41455	-2.1	0.788
		89.2	156251	87.5	36345	-1.7	0.811
		85.7	165408	83.2	35764	-2.5	0.822
		87.0	120487	84.3	44358	-2.7	0.731
		88.7	115454	85.4	50597	-3.3	0.695
AL	11/83	86.3	81364	82.2	51309	-4.1	0.613
		89.1	78020	84.4	53472	-4.7	0.593
		91.0	79561	87.3	47671	-3.7	0.625
		91.6	90066	88.5	45987	-3.1	0.662
		92.3	84762	89.4	44166	-2.9	0.657
		91.8	86832	89.3	46209	-2.5	0.653
		91.6	82727	89.2	46950	-2.4	0.638
		88.9	80236	85.3	50563	-3.6	0.613
		85.5	87779	82.4	47622	-3.1	0.648
		87.4	64905	83.8	43621	-3.6	0.598
		88.6	74330	85.0	57762	-3.6	0.563
KN	11/83	86.1	45427	82.7	78585	-3.4	0.366
		88.8	39293	85.7	53681	-3.1	0.423
		91.1	42790	87.6	70481	-3.5	0.378
		92.7	43846	88.9	82695	-3.8	0.346
		93.3	43442	89.6	80846	-3.7	0.350
	6/83	92.6	45343	90.3	100850	-2.3	0.310
		92.3	46288	88.5	90497	-3.8	0.338
		88.1	49772	85.6	83134	-2.5	0.374
		81.9	62138	80.2	103726	-1.7	0.375
		84.9	31250	82.5	74384	-2.4	0.296
		85.2	53343	84.4	80652	-0.8	0.398

Source: "Petroleum Marketing Monthly," DOE."

TABLE IX

DISTILLATE FUEL OIL
DELIVERIES BY PRIME SUPPLIERS
PAD I

Each Group in Alphabetical Order	1976 Monthly Average Delivery Volumes (barrels)	1976 Percent of State Total	Each Group in Alphabetical Order	1978 Monthly Average Delivery Volumes (barrels)	1978 Percent of State Total
STATE: Connecticut					
TOP FIRMS			TOP FIRMS		
Chevron			Amerada Hess		
Exxon			Chevron		
Mobil			Exxon		
Texaco			Texaco		
Total Top Four	1,474,322	62.13%	Total Top Four	1,344,001	66.01%
Amerada Hess			Gulf		
Gulf			Metropolitan		
Metropolitan			Mobil		
Shell			Royal		
Total Top Eight	2,014,414	84.89%	Total Top Eight	1,721,871	84.56%
Others (11)	358,316	15.11	Others (14)	314,345	15.44
TOTAL STATE	2,372,730	100.00%	TOTAL STATE	2,036,216	100.00%
STATE: Delaware					
TOP FIRMS			TOP FIRMS		
Atlantic Richfield			Atlantic Richfield		
Exxon			Exxon		
Getty			Getty		
Keystone			Keystone		
Total Top Four	225,579	53.99%	Total Top Four	316,091	72.78%
Cities Service			Amoco		
Gulf			Cities Service		
Koch			Sun Oil		
Texaco			Texaco		
Total Top Eight	346,460	82.91%	Total Top Eight	393,907	90.67%
Others (10)	71,379	17.09	Others (9)	40,506	9.33
TOTAL STATE	417,839	100.00%	TOTAL STATE	434,313	100.00%
STATE: District of Columbia					
TOP FIRMS			TOP FIRMS		
Amerada Hess			Amerada Hess		
Atlantic Richfield			Amoco		
BP			Atlantic Richfield		
Texaco			Gulf		
Total Top Four	87,686	78.56%	Total Top Four	131,646	71.63%
Amoco			BP		
Exxon			Exxon		
Gulf			Hessick		
Tenneco			Texaco		
Total Top Eight	111,296	99.7 %	Total Top Eight	176,372	96.27%
Others (3)	340	.3	Others (3)	6.878	3.73
TOTAL STATE	111,636	100.00%	TOTAL STATE	183,810	100.00%

DISTILLATE FUEL OIL
DELIVERIES BY PRIME SUPPLIERS
PAD I

EXHIBIT B-23
(continued)

1976			1978		
Each Group in Alphabetical Order	Monthly Average Delivery Volumes (Barrels)	Percent of State Total	Each Group in Alphabetical Order	Monthly Average Delivery Volumes (Barrels)	Percent of State Total
STATE: Florida					
TOP FIRMS			TOP FIRMS		
Chevron			Amerada Hess		
Gulf			Eastern Seaboard		
Marathon			Phillips		
Phillips			Shell		
Total Top Four	456,349	70.83%	Total Top Four	349,204	47.17%
Amerada Hess			Chevron		
Exxon			Gulf		
Texaco			Marathon		
Triangle			Tenneco		
Total Top Eight	590,260	91.62%	Total Top Eight	588,472	79.49%
Others (11)	53,985	8.38	Others (8)	151,803	20.51
TOTAL STATE	644,245	100.00%	TOTAL STATE	740,275	100.00%
STATE: Georgia					
TOP FIRMS			TOP FIRMS		
Chevron			Amerada Hess		
Gulf			Chevron		
Phillips			Gulf		
Swann			Phillips		
Total Top Four	453,042	62.90%	Total Top Four	380,656	58.01%
Amerada Hess			Amoco		
Amoco			Cities Service		
Marathon			Marathon		
Tenneco			Swann		
Total Top Eight	593,310	82.38%	Total Top Eight	534,247	81.42%
Others (12)	126,896	17.62	Others (12)	121,966	18.58
TOTAL STATE	720,206	100.00%	TOTAL STATE	656,113	100.00%
STATE: Maine					
TOP FIRMS			TOP FIRMS		
Exxon			Exxon		
Gulf			Getty		
Mobil			Mobil		
Northeast Petroleum			Northeast Petroleum		
Total Top Four	622,758	67.70%	Total Top Four	582,907	67.83%
BP			Agway		
Chevron			Chevron		
Shell			Gulf		
Texaco			Texaco		
Total Top Eight	840,450	91.36%	Total Top Eight	816,945	95.07%
Others (6)	79,447	8.64	Others (5)	42,395	4.93
TOTAL STATE	919,897	100.00%	TOTAL STATE	859,340	100.00%

EXHIBIT B-23
(continued)

DISTILLATE FUEL OIL
DELIVERIES BY PRIME SUPPLIERS
PAD I

Each Group in Alphabetical Order	1976 Monthly Average Delivery Volumes (Barrels)	1976 Percent of State Total	Each Group in Alphabetical Order	1978 Monthly Average Delivery Volumes (Barrels)	1978 Percent of State Total
STATE: Maryland					
TOP FIRMS			TOP FIRMS		
Amerada Hess			Amerada Hess		
Atlantic Richfield			Atlantic Richfield		
Exxon			Exxon		
Gulf			Gulf		
Total Top Four	874,988	54.19%	Total Top Four	966,118	60.09%
Amoco Oil			Amoco		
BP			BP		
Shell			Mobil		
Tenneco			Southern States		
Total Top Eight	1,248,084	77.30%	Total Top Eight	1,339,811	83.33%
Others, (14)	366,488	22.70	Others (19)	268,009	16.67
TOTAL STATE	1,614,572	100.00%	TOTAL STATE	1,607,820	100.00%
STATE: Massachusetts					
TOP FIRMS			TOP FIRMS		
Exxon			Exxon		
Northeast Petroleum			Northeast Petroleum		
Texaco			Texaco		
Union			Union		
Total Top Four	2,366,941	57.89%	Total Top Four	2,652,455	65.01%
Atlantic Richfield			Atlantic Richfield		
Gulf			Gulf		
Metropolitan			Metropolitan		
Mobil			Mobil		
Total Top Eight	3,390,209	82.91%	Total Top Eight	3,472,865	85.12%
Others (14)	698,472	17.09	Others (17)	606,979	14.88
TOTAL STATE	4,088,681	100.00%	TOTAL STATE	4,079,844	100.00%
STATE: New Hampshire					
TOP FIRMS			TOP FIRMS		
C. H. Sprague			C. H. Sprague		
Exxon			Exxon		
Northeast Petroleum			Northeast Petroleum		
Shell Oil			Union		
Total Top Four	386,048	59.41%	Total Top Four	364,421	62.77%
Gulf			Gulf		
Mobil			Mobil		
Texaco			Shell		
Union			Texaco		
Total Top Eight	566,235	87.14%	Total Top Eight	532,396	91.70%
Others (8)	83,524	12.96	Others (9)	48,160	8.3
TOTAL STATE	649,759	100.00%	TOTAL STATE	580,556	100.00%

EXHIBIT B-23
(continued)

DISTILLATE FUEL OIL
DELIVERIES BY PRIME SUPPLIERS
PAD I

Each Group in Alphabetical Order	1976 Monthly Average Delivery Volumes (Barrels)	1976 Percent of State Total	Each Group in Alphabetical Order	1978 Monthly Average Delivery Volumes (Barrels)	1978 Percent of State Total
STATE: New Jersey					
TOP FIRMS			TOP FIRMS		
Amerada Hess			Amerada Hess		
Cities Service			Continental Oil		
Continental Oil			Exxon		
Exxon			Gulf		
Total Top Four	2,192,448	43.92%	Total Top Four	2,230,054	46.42%
Chevron			Atlantic Richfield		
Gulf			Che		
Royal			Mobil		
Texaco			Texaco		
Total Top Eight	3,354,168	67.20%	Total Top Eight	3,202,339	66.67%
Others (17)	1,637,460	32.80	Others (23)	1,600,838	33.33
TOTAL STATE	4,991,628	100.00%	TOTAL STATE	4,803,177	100.00%
STATE: New York					
TOP FIRMS			TOP FIRMS		
Exxon			Exxon		
Gulf			Gulf		
Mobil			Mobil		
Northville			Northville		
Total Top Four	3,817,915	43.73%	Total Top Four	4,413,243	50.20%
Amerada Hess			Amerada Hess		
Metropolitan			Cibro Terminals		
Royal			Metropolitan		
Texaco			Royal		
Total Top Eight	5,727,219	65.60%	Total Top Eight	6,382,213	72.59%
Others (24)	3,003,054	34.40	Others (24)	2,409,294	27.41
TOTAL STATE	8,730,272	100.00%	TOTAL STATE	8,791,587	100.00%
STATE: North Carolina					
TOP FIRMS			TOP FIRMS		
Exxon			Amerada Hess		
Gulf			Amoco		
Shell			Exxon		
Sun			Gulf		
Total Top Four	865,931	51.53%	Total Top Four	721,124	42.78%
Amerada Hess			Phillips		
Amoco			Sun		
Phillips			Texaco		
Texaco			Union		
Total Top Eight	1,281,837	76.28%	Total Top Eight	1,116,669	66.37%
Others (16)	398,495	23.72	Others (15)	565,804	33.63
TOTAL STATE	1,680,332	100.00%	TOTAL STATE	1,682,473	100.00%

EXHIBIT B-23
(continued)

DISTILLATE FUEL OIL
DELIVERIES BY PRIME SUPPLIERS
PAD I

1976			1978		
Each Group in Alphabetical Order	Monthly Average Delivery Volumes (Barrels)	Percent of State Total	Each Group in Alphabetical Order	Monthly Average Delivery Volumes (Barrels)	Percent of State Total
STATE: Pennsylvania					
TOP FIRMS			TOP FIRMS		
Atlantic Richfield			Atlantic Richfield		
Exxon			Exxon		
Gulf			Gulf Oil		
Mobil			Texaco		
Total Top Four	2,732,999	50.53%	Total Top Four	2,727,438	48.24%
BP			Amoco		
Cities Service			Cities Service		
Sun			Mobil		
Texaco			Sun		
Total Top Eight	3,987,596	73.73%	Total Top Eight	4,064,425	71.89%
Others (19)	1,421,060	26.27	Others (21)	1,589,512	28.11
TOTAL STATE	5,408,657	100.00%	TOTAL STATE	5,653,937	100.00
STATE: Rhode Island					
TOP FIRMS			TOP FIRMS		
Atlantic Richfield			Getty		
Mobil			Mobil		
Northeast Petroleum			Northeast Petroleum		
Texaco			Texaco		
Total Top Four	478,323	60.68%	Total Top Four	517,209	78.16%
Getty			Amoco		
Gulf			Atlantic Richfield		
Shell			Gulf		
Union			Union		
Total Top Eight	673,410	85.43%	Total Top Eight	641,588	96.96%
Others (8)	114,846	14.57	Others (10)	20,140	3.04
TOTAL STATE	788,256	100.00%	TOTAL STATE	661,728	100.00%
STATE: South Carolina					
TOP FIRMS			TOP FIRMS		
Exxon			Amerada Hess		
Gulf			Exxon		
Shell			Gulf		
Texaco			Shell		
Total Top Four	296,572	53.07%	Total Top Four	400,334	60.91%
Amerada Hess			Amoco		
Amoco			Phillips		
Phillips			Texaco		
Union			Union		
Total Top Eight	439,170	78.50%	Total Top Eight	559,169	85.08%
Others (13)	120,258	21.50	Others (12)	98,363	14.92
TOTAL STATE	559,428	100.00%	TOTAL STATE	657,237	100.00%

EXHIBIT B-23
(continued)

DISTILLATE FUEL OIL
DELIVERIES BY PRIME SUPPLIERS
PAD I

Each Group in Alphabetical Order	1978 Monthly Average Delivery Volumes (Barrels)	1978 Percent of State Total	Each Group in Alphabetical Order	1978 Monthly Average Delivery Volumes (Barrels)	1978 Percent of State Total
STATE: Vermont					
TOP FIRMS			TOP FIRMS		
Exxon			Exxon		
Gulf			Metropolitan		
Mobil			Mobil		
Northeast Petroleum			Northeast Petroleum		
Total Top Four	144,638	54.26	Total Top Four	127,308	55.97%
Agway			Agway		
Royal			Amerada Hess		
Shell			Gulf		
Texaco			Texaco		
Total Top Eight	210,591	79.00%	Total Top Eight	184,584	81.16%
Others (12)	55,970	21.00	Others (12)	42,357	19.34
TOTAL STATE	266,561	100.00%	TOTAL STATE	227,441	100.00%
STATE: Virginia					
TOP FIRMS			TOP FIRMS		
Amoco			Amoco		
Exxon			Atlantic Richfield		
Gulf			Exxon		
Union			Gulf		
Total Top Four	825,329	47.35%	Total Top Four	981,649	49.22%
Atlantic Richfield			BP		
Cities Service			Cities Service		
Shell			Marathon		
Texaco			Phillips		
Total Top Eight	1,252,641	71.86%	Total Top Eight	1,367,370	68.42%
Others (16)	490,419	28.14	Others (20)	631,087	31.58
TOTAL STATE	1,743,060	100.00%	TOTAL STATE	1,998,457	100.00%
STATE: West Virginia					
TOP FIRMS			TOP FIRMS		
Ashland			Amoco		
Exxon			Ashland		
Gulf			Gulf		
Quaker State			Quaker State		
Total Top Four	262,597	75.56	Total Top Four	308,113	76.10%
Amoco			Exxon		
Atlantic Richfield			Southern States Corp.		
Tenneco			Texaco		
Texaco			Union		
Total Top Eight	318,114	91.54%	Total Top Eight	374,730	92.55%
Others (11)	29,418	8.46	Others (13)	30,148	7.45
TOTAL STATE	347,532	100.00%	TOTAL STATE	404,878	100.00%

EXHIBIT B-23
(continued)

DISTILLATE FUEL OIL
DELIVERIES BY PRIME SUPPLIERS
PAD II

1976 Each Group in Alphabetical Order	1976 Monthly Average Delivery Volumes (Barrels)	1976 Percent of State Total	1978 Each Group in Alphabetical Order	1978 Monthly Average Delivery Volumes (Barrels)	1978 Percent of State Total
STATE: Illinois					
TOP FIRMS			TOP FIRMS		
Amoco			Amoco Oil Co.		
Clark			Clark Oil & Ref.		
Marathon			Marathon Oil Co.		
Phillips			Phillips Petroleum		
Total Top Four	1,294,537	59.33%	Total Top Four	1,409,501	57.96%
Shell			Apel Oil Co.		
Sun			Mobil Oil Corp.		
Texaco			Shell Oil Co.		
Union			Texaco Inc.		
Total Top Eight	1,734,277	79.48%	Total Top Eight	1,969,393	80.77%
Others (19)	436,406	20.52	Others (21)	467,689	19.23
TOTAL STATE	2,182,029	100.00%	TOTAL STATE	2,432,083	100.00%
STATE: Indiana					
TOP FIRMS			TOP FIRMS		
Amoco			Amoco Oil Co.		
Indiana Farm Bureau			Marathon Oil Co.		
Marathon			Rock Island Refining		
Rock Island			Shell Oil Co.		
Total Top Four	994,967	56.5 %	Total Top Four	1,246,165	52.9 %
Gladieux Refinery			Cities Service		
Phillips			Clark Oil & Ref.		
Shell Oil			Indiana Farm Bureau		
Sun Oil			Phillips Petroleum Co.		
Total Top Eight	1,298,106	73.71%	Total Top Eight	1,670,350	71.04%
Others (17)	462,993	26.29	Others (16)	680,930	28.96
TOTAL STATE	1,761,099	100.00%	TOTAL STATE	2,351,281	100.00%
STATE: Iowa					
TOP FIRMS			TOP FIRMS		
Amoco			Amoco		
Farmland			Farmland		
Phillips			Phillips		
Sun			Sun		
Total Top Four	332,901	49.22%	Total Top Four	393,830	50.6 %
Continental			FS Services		
Koch			Getty Ref.		
Mobil			Mobil		
Skelly			Shell Oil Co.		
Total Top Eight	473,812	70.06%	Total Top Eight	568,795	73.08%
Others (19)	202,483	29.94	Others (18)	209,523	26.92
TOTAL STATE	676,295	100.00%	TOTAL STATE	778,318	100.00%

EXHIBIT B-23
(continued)

DISTILLATE FUEL OIL
DELIVERIES BY PRIME SUPPLIERS
PAD II

Each Group in Alphabetical Order	1976 Monthly Average Delivery Volumes (Barrels)	1976 Percent of State Total	Each Group in Alphabetical Order	1978 Monthly Average Delivery Volumes (Barrels)	1978 Percent of State Total
STATE: Kansas					
TOP FIRMS			TOP FIRMS		
APCO			Amoco Oil Co.		
Derby			Apex Oil Co.		
National Coop.			Derby Refining Co.		
Phillips			Phillips Petroleum Co.		
Total Top Four	251,966	73.13%	Total Top Four	221,870	63.93%
Amoco			Farmland Ind.		
Farmland Industries			Getty Refining		
Mobil			Koch Ref.		
Skelly			Total Petroleum Inc.		
Total Top Eight	321,777	94.38%	Total Top Eight	310,629	89.46%
Others (11)	19,161	5.62	Others (12)	36,598	10.54
TOTAL STATE	340,938	100.00%	TOTAL STATE	347,227	100.00%
STATE: Kentucky					
TOP FIRMS			TOP FIRMS		
Ashland			Ashland		
Chevron			Chevron		
Gulf			Gulf		
Texaco			Marathon		
Total Top Four	297,082	69.86%	Total Top Four	403,415	65.53%
Marathon			Shell		
Phillips			Sun Oil		
Shell			Texaco		
Triangle			Triangle		
Total Top Eight	390,625	91.86%	Total Top Eight	582,629	98.76%
Others (11)	34,614	8.14	Others (15)	63,045	10.24
TOTAL STATE	425,239	100.00%	TOTAL STATE	615,674	100.00%
STATE: Michigan					
TOP FIRMS			TOP FIRMS		
Amoco			Amoco Oil		
Marathon			Marathon Oil		
Mobil			Mobil		
Total			Total		
Total Top Four	933,207	59.98%	Total Top Four	937,969	58.61%
Gulf			Cities		
Shell			Clark		
Sun			Shell		
Union			Union		
Total Top Eight	1,279,805	82.25%	Total Top Eight	1,284,071	77.27%
Others (17)	275,999	17.74	Others (21)	377,727	22.73
TOTAL STATE	1,555,805	100.00%	TOTAL STATE	1,661,798	100.00%

EXHIBIT B-23
(continued)

DISTILLATE FUEL OIL
DELIVERIES BY PRIME SUPPLIERS
PAD II

Each Group in Alphabetical Order	1976 Monthly Average Delivery Volumes (Barrels)	1976 Percent of State Total	Each Group in Alphabetical Order	1978 Monthly Average Delivery Volumes (Barrels)	1978 Percent of State Total
STATE: Minnesota					
TOP FIRMS			TOP FIRMS		
Amoco			Amoco		
Farmers Union			Koch		
Koch			Mobil		
Phillips			Phillips		
Total Top Four	940,653	61.68%	Total Top Four	1,039,333	63.47%
Continental			Ashland		
Midland Corp.			Continental		
Mobil			Farmers Union		
Union Oil			Midland		
Total Top Eight	1,196,378	78.45%	Total Top Eight	1,319,514	36.58%
Others (18)	328,642	21.55	Others (18)	319,007	19.42
TOTAL STATE	1,525,019	100.00%	TOTAL STATE	1,637,521	100.00%
STATE: Missouri					
TOP FIRMS			TOP FIRMS		
Amoco			Amoco		
Phillips			Getty		
Shell			Phillips		
Skelly			Shell		
Total Top Four	330,477	50.65%	Total Top Four	447,624	54.11%
Clark			Clark		
MFA			Gulf		
Mobil			Mobil		
Sun			Sun		
Total Top Eight	478,870	73.41%	Total Top Eight	627,092	75.81%
Others (17)	173,489	26.59	Others (16)	200,097	24.19
TOTAL STATE	652,459	100.00%	TOTAL STATE	827,189	100.00%
STATE: Nebraska					
TOP FIRMS			TOP FIRMS		
Amoco			Amoco		
Farmland Ind.			Farmland		
Phillips			Getty		
Skelly			Phillips		
Total Top Four	181,387	60.16%	Total Top Four	213,456	61.73%
Continental			Continental		
Mobil			Kerr-McGee		
Sun			Land o'Lakes		
Texaco			Mobil		
Total Top Eight	255,623	84.77%	Total Top Eight	288,753	83.5
Others (13)	45,926	15.23	Others (16)	57,059	16.5
TOTAL STATE	301,549	100.00%	TOTAL STATE	345,911	100.00%

DISTILLATE FUEL OIL
DELIVERIES BY PRIME SUPPLIERS
PAD II

EXHIBIT B-23
(continued)

1976 Each Group in Alphabetical Order	1976 Monthly Average Delivery Volumes (Barrels)	1976 Percent of State Total	1978 Each Group in Alphabetical Order	1978 Monthly Average Delivery Volumes (Barrels)	1978 Percent of State Total
STATE: North Dakota					
TOP FIRMS			TOP FIRMS		
Amoco			Amoco		
Farmers Union			Ashland		
Koch			Farmers Union		
Mobil			Mobil		
Total Top Four	176,386	65.01%	Total Top Four	171,564	66.19%
Ashland			Farmland		
Farmland Industries			Kerr-McGee		
Gulf			Phillips		
Texaco			Texaco		
Total Top Eight	229,775	84.68%	Total Top Eight	221,298	85.38%
Others (12)	41,698	15.32	Others (16)	37,894	14.62
TOTAL STATE	271,473	100.00%	TOTAL STATE	259,192	100.00%
STATE: Ohio					
TOP FIRMS			TOP FIRMS		
Ashland			Ashland		
Boron			Boron		
Gulf			Landmark		
Marathon			Marathon		
Total Top Four	1,495,164	70.76%	Total Top Four	1,556,413	60.92%
Mobil			Gulf		
Shell			Mobil		
Sun			Shell		
Union			Union		
Total Top Eight	1,816,142	85.95%	Total Top Eight	2,000,820	78.33%
Others (17)	296,880	14.05	Others (18)	553,527	21.67
TOTAL STATE	2,113,022	100.00%	TOTAL STATE	2,554,347	100.00%
STATE: Oklahoma					
TOP FIRMS			TOP FIRMS		
Amoco			Apex		
Farmland			OKC		
Phillips			Phillips		
Shell			Sun		
Total Top Four	45,330	73.22%	Total Top Four	234,523	78.70%
Apco			Amoco		
Gulf			Farmland		
Sun			Koch		
Vickers			Total		
Total Top Eight	55,740	90.03%	Total Top Eight	284,825	95.58%
Others (8)	6,173	9.97	Others (14)	13,171	4.42
TOTAL STATE	61,913	100.00%	TOTAL STATE	297,996	100.00%

DISTILLATE FUEL OIL
DELIVERIES BY PRIME SUPPLIERS
PAD II

EXHIBIT B-23
(continued)

Each Group in Alphabetical Order	1976 Monthly Average Delivery Volumes (Barrels)	1976 Percent of State Total	Each Group in Alphabetical Order	1978 Monthly Average Delivery Volumes (Barrels)	1978 Percent of State Total
STATE: South Dakota					
TOP FIRMS			TOP FIRMS		
Amoco			Amoco		
Farmers Union			Farmers		
Farmland			Farmland		
Mobil			Mobil		
Total Top Four	114,943	64.52%	Total Top Four	120,300	60.55%
Kerr-McGee			Getty		
Phillips			Phillips		
Skelly			Sun		
Texaco			Texaco		
Total Top Eight	151,103	84.83%	Total Top Eight	161,813	81.44%
Others (11)	27,021	15.17	Others (16)	36,877	19.56
TOTAL STATE	178,124	100.00%	TOTAL STATE	198,690	100.00%
STATE: Tennessee					
TOP FIRMS			TOP FIRMS		
Exxon			Amoco		
Gulf			Exxon		
Phillips			Gulf		
Shell			Phillips		
Total Top Four	391,534	71.18%	Total Top Four	401,409	78.46%
Amoco			Chevron		
Atlantic Richfield			Mobil		
Mobil			Shell		
Sun			Tenneco		
Total Top Eight	480,009	87.25%	Total Top Eight	465,200	90.93%
Others (13)	80,145	12.75	Others (8)	56,402	9.17
TOTAL STATE	560,154	100.00%	TOTAL STATE	521,602	100.00%
STATE: Wisconsin					
TOP FIRMS			TOP FIRMS		
Amoco			Amoco		
Koch			Koch		
Shell			Marathon		
Texaco			Texaco		
Total Top Four	652,430	45.65%	Total Top Four	694,841	44.05%
Clark			Cities		
Farmers Union			Clark		
Marathon			Midland		
Mobil			Mobil		
Total Top Eight	987,752	69.11%	Total Top Eight	1,091,523	69.20%
Others (19)	451,494	30.89	Others	495,822	30.80
TOTAL STATE	1,439,246	100.00%	TOTAL STATE	1,587,354	100.00%

EXHIBIT B-23
(continued)

DISTILLATE FUEL OIL
DELIVERIES BY PRIME SUPPLIERS
PAD III

Each Group in Alphabetical Order	1976 Monthly Average Delivery Volumes (Barrels)	1976 Percent of State Total	Each Group in Alphabetical Order	1978 Monthly Average Delivery Volumes (Barrels)	1978 Percent of State Total
STATE: Alabama					
TOP FIRMS			TOP FIRMS		
Amerada Hess			Amerada Hess		
Chevron			Chevron		
Exxon			Hunt		
Hunt			Phillips		
Total Top Four	129,213	76.09%	Total Top Four	124,699	74.61%
Phillips			Atlantic		
Shell			Exxon		
Tenneco			Shell		
Union			Tesoro		
Total Top Eight	156,638	92.24%	Total Top Eight	156,158	93.42%
Others (10)	13,178	7.76	Others (11)	10,999	6.58
TOTAL STATE	169,316	100.00%	TOTAL STATE	167,157	100.00%
STATE: Arkansas					
TOP FIRMS			TOP FIRMS		
Continental			Apex		
Exxon			Farmland		
Farmland			Phillips		
Phillips			Sun		
Total Top Four	61,136	96.01%	Total Top Four	104,430	89.12%
Amoco			Amoco		
Apco			Atlantic		
Gulf			Exxon		
Sun			Total		
Total Top Eight	66,467	99.56%	Total Top Eight	115,434	98.51%
Others (7)	289	.44	Others (11)	1,746	1.49%
TOTAL STATE	66,756	100.00%	TOTAL STATE	117,180	100.00%
STATE: Louisiana					
TOP FIRMS			TOP FIRMS		
Apex			Apex	247,913	
North American Petro			North American Petro	129,666	
Phillips			Shell	53,288	
Sun			Tenneco	25,469	
Total Top Four	192,146	89.42%	Total Top Four	482,305	93.36%
Exxon			Exxon		
Gulf			Hill		
Shell			Phillips		
Tenneco			Tesoro		
Total Top Eight	212,221	98.77%	Total Top Eight	554,069	96.34%
Others (8)	2,643	1.23	Others (13)	17,470	3.66
TOTAL STATE	214,864	100.00%	TOTAL STATE	571,569	100.00%

EXHIBIT B-23
(continued)

DISTILLATE FUEL OIL
DELIVERIES BY PRIME SUPPLIERS
PAD III

Each Group in Alphabetical Order	1976 Monthly Average Delivery Volumes (Barrels)	1976 Percent of State Total	Each Group in Alphabetical Order	1978 Monthly Average Delivery Volumes (Barrels)	1978 Percent of State Total
STATE: Mississippi					
TOP FIRMS			TOP FIRMS		
Chevron			Chevron		
Gulf			Ergon		
Phillips			Phillips		
Tennoco			Shell		
Total Top Four	97,999	83.44%	Total Top Four	124,185	79.38%
Amerada Hess			Amerada Hess		
Amoco			Amoco		
Clark			Gulf		
Shell			Sun		
Total Top Eight	114,130	97.18%	Total Top Eight	148,238	94.75%
Others (6)	3,312	2.82	Others (6)	8,214	5.25
TOTAL STATE	117,442	100.00%	TOTAL STATE	156,452	100.00%
STATE: New Mexico					
TOP FIRMS			TOP FIRMS		
Caribou Four Corners			Amoco		
Chevron			Getty		
Gulf			Gulf		
Phillips			Phillips		
Continental			Chevron		
Farmland			Continental		
Texaco			Farmland		
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Total Top Eight	25,004	100.00%	Total Top Eight	43,109	100.00%
Others (none)	-0-	-0-	Others (none)	-0-	-0-
TOTAL STATE	25,004	100.00%	TOTAL STATE	43,109	100.00%
STATE: Texas					
TOP FIRMS			TOP FIRMS		
Atlantic Richfield			Charter		
Charter			Howell		
Phillips			Phillips		
Shell			Shell		
Total Top Four	425,438	73.79%	Total Top Four	1,688,753	79.53%
Marathon			Amoco		
Pride			Apex		
Sun			Marathon		
Texaco			Pride		
Total Top Eight	517,985	89.84%	Total Top Eight	2,038,038	95.97%
Others (19)	58,579	10.16	Others (19)	85,582	4.03
TOTAL STATE	576,564	100.00%	TOTAL STATE	2,123,620	100.00%

A Prime Supplier, as defined by the U.S. Department of Energy, is "the supplier...which makes the first sale of an allocated product subject to state set-aside...for consumption within the state."

SOURCE: EIA 25 Survey, "Prime Suppliers Monthly Report", Energy Information Administration, U.S. Department of Energy.

Senator HATCH. Mr. Story?

Mr. STORY. Thank you, sir.

I am speaking today for myself and not for Wharton Econometrics. My position with Wharton is as international oil analyst and forecaster. In that sense, I have tried to look into the implications of the mergers in the United States in terms of the impact on the international oil market. I am afraid I have not found very much in the way of evidence of any impact—with one exception.

While I believe Mr. Tavoulareas and Mr. Keller when they say they will devote as much money to exploration and development of oil after the merger as before, I have seen evidence of the mergers in recent years where this is not necessarily the case.

Oil companies after a merger are going to have a fixed amount of money to spend on their operations in a given year, and if they have very large sums of money to pay back in terms of interest, based on the acquisition of a new company, they are not going to have as much money as they would otherwise, and they will have to cut somewhere. In some cases, this leads to some efficiencies through efficiencies of scale. You will see them selling off some parts of the companies that they do not think fit into the new operation after the merger. But on balance, you probably will not find as much money in the combined firm going into exploration and development as you would have otherwise.

And an important thing that has not been mentioned too much today is how much of this exploration and development money is going abroad in addition to being invested in the United States, looking for new oil.

A related point that I have not really heard mentioned here today is the reason, one of the major reasons—of course, everybody agrees that these mergers have taken place—is the value of U.S. reserves as opposed to reserves involved in places like the Middle East and around the world. In fact, probably the safest oil in place, undiscovered, is definitely in the United States and in the North Sea. I think you would agree with most of the experts in this field who say that U.S. reserves are going down, along with U.S. production, through the end of this decade. What this means is there should be a greater effort to explore abroad, to supplement U.S. reserves and production in the future, to help us in terms of our energy security over time.

Having said this, I will be happy to not use my next 2 minutes.

Senator HATCH. Thank you so much.

I want to thank each of the four of you for appearing.

We appreciate the testimony the witnesses have brought with them and the statements they have made, and with that, we will recess these hearings until further notice.

Senator METZENBAUM. These are good witnesses, and I am really embarrassed that they are called upon to be heard at such a late hour, but we appreciate what you have said—since you agree with us.

Senator HATCH. Thank you very much.

[Whereupon, at 8:06 p.m., the committee was adjourned.]

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